ask the expert

PMI EXPERT PARTNER

LEGAL

To what extent are trustee boards' investment policies constrained by the Cowan v Scargill case?

Ferdinand Lovett
Solicitor
Sacker & Partners LLP

Judging by the website traffic to our summary of the 1984 Cowan v Scargill case on trustees' investment duties, this is a question that continues to generate a significant amount of interest amongst trustees.

What is the Cowan v Scargill duty?

Pension scheme trust deeds and rules will typically confer upon pension trustees wide powers of investment. However, exercise of these investment powers is underpinned by the general trust law duty that pension trustees are to act in the best interests of scheme beneficiaries.

This was the point considered in the Cowan v Scargill case where the Court held that, in the context of investment decisions, "best interests" meant the beneficiaries' best **financial** interests.

What was Cowan v Scargill about?

It concerned a mineworkers' pension scheme set up by the National Coal Board (NCB). The scheme's committee of management comprised trustees appointed by the NCB and trustees appointed by the National Union of Mineworkers (NUM). When, in 1982, the NCB proposed investments in oil, overseas investments and the acquisition of land overseas, the NUM trustees took issue with the proposals on the basis that they believed they went against NUM policy. The issue escalated and the NCB trustees sought directions from the Court as to whether the NUM trustees were in breach of their fiduciary duties in resisting the adoption of the 1982 investment proposals.

The Court held that they were, stating that *"the starting point is the duty of trustees to exercise their powers in the best interests of the present and future beneficiaries of the trusts… When the purpose of the trust is to provide financial benefits for the beneficiaries …the best interests of the beneficiaries are normally their best financial interests"*.

Additional guidelines from the judgment include:

- in considering what investments to make, trustees must put aside personal interests and views
- if all the beneficiaries of a trust are adults with strict views on moral issues then it might not be to the 'benefit' of those beneficiaries to invest in something inimical to those views. But, such cases are likely to be very rare

The effects on today's trustee boards

The Cowan v Scargill principles remain 'good law', with the need to consider pension scheme beneficiaries' best financial interests remaining of paramount importance for trustees. To that extent the Cowan v Scargill principles do continue to "constrain" trustee board investment policies.

However, the issue of pension scheme investment is far from straightforward and is an area that attracts attention from various quarters, most recently from the Law Commission in its report to Parliament on *"Fiduciary Duties of Investment Intermediaries"*.

> The issue of pension scheme investment is far from straightforward and is an area that attracts attention from most quarters

Considering ESG factors when investing

The Law Commission restates in its 2014 report the key duty of trustees to invest in members' best interests. It shrinks however from stating that this equates to investment policies being driven purely by absolute maximisation of financial returns.

It suggests that environmental, social and governance (ESG) factors can be taken into account by trustees when weighing up investment decisions, if they constitute "financial factors". Further, any financially material factors **must** be considered.

However, according to the report, "non-financial" factors should only be taken into account if trustees have good reason to think that scheme members would share the concern and the decision does not involve a risk of significant financial detriment to the fund.

The majority of pension schemes are established to provide specific financial benefits without any express social aim or purpose. As such, trustees should in most cases continue to look to invest in members' best financial interests while – as with any discretionary decision – taking into account relevant factors and ignoring irrelevant ones.

Looking forward

The Law Commission has recommended that the Pensions Regulator considers how best to give greater exposure and authority to the guidance contained in the report. It has also recommended that the Government amend the Occupational Pension Schemes (Investment) Regulations 2005 to "distinguish more clearly between financial and non-financial factors". One to watch.

Sackers