How public pension funds can help address climate change

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With public pension funds managing $4 trillion nationally and essentially representing the retirement plans of 20 million U.S. workers, where that money is invested has a lot of ramifications.

In recent years, attention has focused on the fossil fuel industry, where public pension fund investors play a growing role.

As Michael McCann, political science professor at the University of Washington, and Riddhi Mehta-Neugebauer, a graduate student in political science and former research director for the UW Harry Bridges Center for Labor Studies, point out, private equity firms—including the Blackstone Group, KKR and the Carlyle Group—own and are expanding fossil fuel operations such as pipelines and gas- and coal-fired power plants. Meanwhile, reports from the International Energy Agency and the U.N. Intergovernmental Panel on Climate Change provide dire warnings about global warming.

"It is time that private equity also acts upon information the rest of the world seems to already understand," said Mehta-Neugebauer. "Willfully expanding fossil fuel infrastructure amid intensifying opposition exposes pension fund investors and retirees to investment risks, and exposes all of us to more dangerous climate and public health outcomes."

Ahead of the U.N. Climate Change Conference that begins Oct. 31, the Harry Bridges Center released a report on the issue, following a spring panel discussion with representatives from labor, public pension funds, Indigenous groups and grassroots organizations around North America. The goal: collaboration and change.

McCann and Mehta-Neugebauer discussed the relationship among public pension funds, private equity and climate change with UW News.

What do you think people overlook, or perhaps don't even know, about this issue? And what are the consequences?

RMN: Private equity firms benefit immensely from a structure of secrecy. Through regulatory exemptions, private equity assets are, by definition, private and not subject to most public disclosure rules, like other publicly listed companies such as Chevron or ExxonMobil. As a result, neither the public nor government regulators fully understand the environmental and community impacts of private equity investments.

At the same time, private equity firms extoll their commitment to environmental and sustainable goals, but they fail to disclose the thousands of miles of oil and gas pipelines they manage, or the acres of oil wells they own, or the extent to which communities and ecosystems are impacted by their operations. Thus, private equity's pension fund investors do not have an accurate understanding of the public health and climate risks associated with private equity's ever-expanding fossil fuel footprint and run the risk of making investment decisions based on inaccurate and incomplete information—a serious fiduciary risk.

Riddhi Mehta-Neugebauer

For instance, the same day that private equity firm Brookfield Asset Management raised $7 billion for a new clean energy fund, its $6.7 billion bid to takeover Inter Pipeline, an oil sands pipeline company, was recommended by the company's board for shareholder approval. Brookfield failed to discuss this connection, and very few industry analysts observed how Brookfield's attempts to mitigate climate change were immediately nullified.

Systematic, detailed and comprehensive disclosure of private equity portfolio's climate risks, and plans to shift toward a pollution-free energy portfolio are necessary to enable the public, investors and regulatory agencies to effectively monitor and mitigate negative financial risks as well as climate and health impacts.

Financial returns are often considered the priority for investments, but you argue not only that other issues are important, but also that private equity investment in the fossil fuel industry is risky. Can you explain?

MM: The majority of private equity energy funds have underperformed comparable buyout funds over the past decade. On the other hand, over a similar period, renewable energy stocks beat a fossil fuel-focused strategy by more than threefold. Yet total investment in renewable energy assets is still lagging. And the heavy debt that private equity firms typically load onto their portfolio companies resulted in private equity-owned oil and gas companies dominating the unusually high number of bankruptcies in the energy sector last year.

Looking to the future, major oil companies are acknowledging a permanent decline in oil demand. In February 2021, Royal Dutch Shell joined other major oil companies in saying that the world reached peak oil production in 2019, and going forward, it expects annual declines. Governments and auto manufacturers are also responding to the writing on the wall, setting 2035 as a goal: California, one of the largest markets for vehicle sales, established that target for a phaseout of gasoline-powered cars; the United Kingdom mandated that any car sold after 2030 must have at least a hybrid drivetrain capable of running on a battery; and General Motors announced plans to completely phase out vehicles using internal combustion engines by 2035. GM also plans to use renewable energy for its U.S. factories by 2035, and for overseas plants by 2040.

How can labor unions—or any of us—be part of the solution?

MM: Public pension funds are essentially labor's retirement capital. Investment decisions are made by pension fund trustees, who are often union members, state elected representatives, and investment experts. These trustees can demand robust climate risk reporting standards that take community and environmental impacts into account. Assessing a private equity fund's performance by financial benchmarks alone underestimates the full costs associated with these energy investments.

RMN: Labor unions can do a better job of committing resources to educating themselves and their trustee representatives on how their pension fund invests their retirement capital. Workers and retirees can demand from their pension funds more transparent climate-related disclosures as a condition for future private equity funding.

MM: Much political analysis has focused on the reluctance of labor organizations to fully support a clean energy future. However, greater engagement of labor within the pension fund investment sphere can bring about an alliance between labor and environmental interests. Better understanding the climate risks associated with private equity investments can help protect not only the environment, but also investment returns—ensuring a more sustainable future for retirees as well as the planet.

As the climate crisis impacts all of us, we can also engage on this issue by providing comment at pension fund meetings—after all, they are open to the public. And we can demand that our elected representatives take bolder climate-related actions. Aside from ensuring public pension fund investments are made more responsibly, we all have a stake in ensuring a healthier planet.

Provided by University of Washington

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