

Consultation: Taking action on climate risk

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Introduction

On 26 August 2020, the DWP published a [consultation](#) on pension schemes' governance and reporting on climate change. Initially, the proposed changes will be targeted at larger schemes, which will need to comply from October 2021. The proposals would require schemes to assess and manage climate risks and opportunities, and to publish a climate change report annually (in line with recommendations by the Taskforce on Climate-related Financial Disclosures ("TCFD")).

Key points

- Schemes with £5 billion or more in assets, [authorised master trusts](#) and [authorised collective money purchase schemes](#) ("CMPS") would need to have arrangements in place on climate change governance, strategy, risk management, metrics and targets from October 2021, and to publish an annual report on these by the end of 2022 at the latest.
- This requirement would then be rolled out to schemes with £1 billion or more of assets the following year. Application to smaller schemes will be reviewed in 2024.
- Compliance would be reported to TPR through the annual scheme return.
- The proposed requirements would be enacted under [amendments to the Pension Schemes Bill](#), though these are yet to be passed. A further consultation on regulations will follow "in late 2020 or early 2021".
- The consultation does not include requirements to report on alignment with the Paris Agreement or the "implied temperature rise" of scheme portfolios. The Government "is minded to take steps to require that pension scheme trustees do this", and this will be consulted on "in the near future".

TCFD recommendations

In 2017, the TCFD published 11 recommendations for all organisations, aimed at identifying, assessing, managing and disclosing climate-related financial risks and opportunities. In March 2020, the Pensions Climate Risk Industry Group launched a consultation on guidance on applying the TCFD recommendations to a pension scheme (see our [ESG guide](#)). The final guidance is expected "at the end of 2020".

The DWP proposes that regulations require trustees to satisfy the 11 recommendations of the TCFD, and to report on how they have done so. Statutory guidance would support schemes in achieving this, and trustees would need to explain any divergence from that guidance in their reporting.

The proposed requirements for satisfying the 11 TCFD recommendations are split between four areas:

- **Governance:** establish and maintain, on an ongoing basis, oversight of climate-related risks and opportunities, and processes by which trustees satisfy themselves that persons managing the scheme are assessing and managing those risks and opportunities.
- **Strategy:** identify, on an ongoing basis, climate-related risks and opportunities that will have an effect on the investment and, in the case of DB schemes, funding strategy, over the short, medium and long term, and assess the impact of those risks and opportunities. Schemes would be required to use scenario analysis at least annually to assess the scheme's resilience to climate-related risks.
- **Risk management:** adopt and maintain, on an ongoing basis, processes for identifying, assessing and managing climate-related risks, and integrating climate-related risks into the trustees' overall risk management.
- **Metrics and targets:**
 - select at least one appropriate greenhouse gas emissions-based metric and at least one other non-emissions-based metric, calculating them quarterly to assess scheme assets against climate-related risks and opportunities (and keep the metric selections under review).
 - at least annually, set at least one target for one of the metrics calculated above and measure against the target(s) at least quarterly.

For each of the above areas, the consultation puts forward governance requirements and obligations to disclose against those requirements (which will be set out in regulations). It also proposes areas to be covered by supporting regulatory guidance, to which trustees will need to have regard.

The DWP acknowledges that trustees are dependent on data from other parts of the investment chain. Therefore, initially, trustees will need to comply with requirements on scenario analysis, calculating metrics and reporting against targets "as far as they are able".

Timing

If implemented, the proposals will be phased in, with larger schemes being the first required to comply.

Schemes with assets ≥ £5bn, authorised master trusts and authorised CMPS:

- must meet governance requirements for the current scheme year from 1 October 2021 to the end of that scheme year, and
- must publish a TCFD report on the scheme's or scheme sponsor's website within 7 months of the end of that scheme year or by 31 December 2022 (if earlier), and a link must be included in the Annual Report and Accounts for that scheme year and in annual benefit statements.

Schemes with assets < £5bn but ≥ £1bn: the requirements above to apply one year later.

Schemes would remain in scope until assets fall below £500 million at scheme year end. The requirements would apply to authorised master trusts and CMPS from the point of authorisation and fall away from the point of de-authorisation.

The position for schemes with assets < £1bn will be reviewed in 2024.

Trustees would have to provide TPR with the web address of their TCFD report via the annual scheme return form. The DWP also proposes that trustees would be required to provide a link to their SIP, implementation statement (where applicable) and published excerpts of the chair's statement.

Penalties

A separate penalty regime would be introduced for non-compliance with the proposed governance and reporting requirements. A mandatory penalty, of at least £2,500, is proposed only for complete failure to publish any TCFD report. Other penalties would be subject to TPR discretion. The maximum penalty for breach of any of the requirements would be £5,000 for an individual trustee, or £50,000 for a corporate trustee.

Requirements to reference the TCFD report in the Annual Report, and to inform members about the TCFD report's availability, would be subject to the existing penalty regime on disclosure of information. Failure in relation to TPR notification requirements would be subject to civil penalties up to £5,000 in the case of an individual, and £50,000 in any other case.

Next steps

The consultation runs until 7 October 2020. The proposals are based on amendments made to the Pension Schemes Bill during its passage through the House of Lords. We do not have a timeline for the Bill being passed, and the amendments would have to survive the remaining Parliamentary stages. The Government seems confident that will be the case, and currently plans to consult on regulations "in late 2020 or early 2021".

If the consultation proposals are adopted, TPR will "give consideration to whether those trustees who meet the requirements set out in [the] regulations should be deemed to have also met the standards" in the [forthcoming Governance code](#), insofar as they relate to climate change.