A plan for ESG and climate change integration – from behind the curve to getting ahead

Action plan	Behind the curve Unlikely to stand up to any serious scrutiny	Getting compliant Putting ESG on the agenda
Your action plan		
1 Set investment beliefs	Trustee board relies on its investment consultants to tell them what to believe. Sets nothing out in writing.	Trustee board receives a brief training session before minuting that ESG and climate change are considered material financial factors.
2 Review existing managers	No engagement with existing managers.	Takes stock of existing managers and uses investment consultant scoring framework to rate current managers on their ESG credentials. However, scores are only used as a differentiator where there are other reasons to review a manager.
3 Set a DB investment strategy	Existing strategy not reviewed.	Trustees keep existing strategy under review as ESG experience develops.
4 Consider DC benefits	Does not consider ESG in default fund. Falls into the DC "trap" considering the provision of an "ethical fund" as a self-select option to be sufficient.	Reviews default fund. Manager expected to demonstrate ESG credentials. For passive funds, this may be limited to more active stewardship.
5 Document a policy	Added generic wording to SIP in 2019 at suggestion of the investment consultant in the belief that this will make the trustee "compliant". Will do the same in 2020. Trustees do not consider wording or how it will be implemented in practice.	Trustees considered wording in the SIP in 2019 reflecting the circumstances of the scheme and existing manager mandates. Intend to do a fuller review in 2020. Trustees agree how wording is implemented in practice with their investment consultants.
Further considerations		
Monitor manager	Reports on quarterly past performance figures only. No forward looking consideration of manager ESG attributes or exposure of mandates to climate change risk in the longer term.	Expects active managers to demonstrate how ESG criteria are being used in stock selection and de-selection.
Appointing new managers	Mentions ESG only as an afterthought in tender invitations and gives it no weight in selection criteria.	ESG is identified in tenders as an important issue on which potential new managers will be expected to demonstrate competency.
Stewardship and engagement	Not considered relevant. Justified based on an incorrect assumption that the scheme's investments are all pooled and therefore "stewardship is impossible".	Trustees expect managers to report on how they have exercised voting rights attached to shares (including across passive equity mandates). Managers are expected to be signatories to the FRC UK Stewardship Code.
Climate scenario analysis	None.	Obtains broad estimates from consultants as to the potential significance of climate change on the scheme's portfolio.
Reporting	Sends stock wording to any members "causing a nuisance". Will worry about implementation statements when required.	Some commentary provided to scheme members in annual report. Actively considering implementation statement content now.
Industry involvement	None.	Relies on advisers to provide updates on significant developments, requiring action and training as needed.

On the front foot Embedding ESG into trustee governance	Getting ahead Making ESG and climate change a key strategic issue
Trustee board spends time on training before discussing and agreeing a responsible investment beliefs statement, including a position on climate change risk.	Trustee board discusses ESG beliefs at least annually. Where applicable, trustees seek to align beliefs with sponsor views. Considers alignment of strategy with UN Sustainable Development Goals.
Full consideration of each manager's ESG capabilities (including qualifications) with specialist input from investment consultants – includes being alive to "green-washing". Managers which require most attention identified and engaged with. Where no improvement is forthcoming, or possible within current mandates, these will be reviewed.	Expects all managers to demonstrate deep ESG integration. Integrates corporate environmental data in manager investment processes.
For active mandates: considers diversification across sources of climate risk as well as traditional asset classes. Sustainability and low-carbon indices considered for passive allocations.	Positive allocation to sustainable investment or investment in assets aligned with a below 2˚C pathway. Consider tilting portfolio away from lower scoring ESG assets or sectors such as high carbon emitters.
Reviews composition of DC default to manage ESG risks and align with trustees' ESG beliefs. Regularly reports to members on how default fund is responding to climate change.	Uses ESG leaders or factor-based funds as default. Self-select fund choices include "impact" investment funds with ESG goals. Considers seeking member views to ensure an appropriate fund range.
Trustees develop a stand-alone responsible investment policy which supplements the SIP. This may start with existing manager mandates but will progress to deeper integration of ESG factors over time. The policy identifies priority ESG themes and is periodically reviewed.	Extensive responsible investment policy with detailed consideration of ESG in each asset class, detailed climate change policy and stewardship policies. Climate change risk embedded across other trustee governance and internal control frameworks and considered as part of an integrated risk management framework (including any climate change risks pertinent to the scheme sponsor covenant).
Develops a robust monitoring process – reporting qualitatively and quantitively against each manager. Managers expected to demonstrate integration of ESG in investment processes rather than the existence of separate "advisory" ESG analysts.	Managers expected to provide frequent concrete examples of deep ESG integration and active behaviours with investee companies. Measures alignment of listed equity and corporate bond portfolios across 2˚ transition sectors and technologies.
ESG credentials key in tender process. Investment management agreements negotiated to include specific ESG requirements.	Responsible investment requirements included across all asset classes eg side letter terms in private equity funds.
Expects managers to report in detail on their engagement policies and how these have been implemented. This should include examples of engagement changing corporate behaviours and voting against the board on ESG-related issues. Managers with a poor engagement record will be downgraded. Considers adoption of an off-the-shelf voting policy eg AMNT Red Lines.	Large schemes: takes an active and direct role engaging with investee companies across all asset classes. Considers joining other investors in filing climate-related shareholder resolutions where companies are underperforming on adaptation or disclosure. Scheme is an FRC UK Stewardship Code signatory. Small schemes: appoints proxy voting and engagement service reflecting trustees' ESG beliefs and position on climate risk.
Makes use of freely available tools such as PACTA and / or PRA stress test data.	All-portfolio risk assessment (including all real asset holdings) to identify exposure to transition risks and potential physical damage risk under different climate scenarios.
Considers TCFD reporting framework as a structure for internal governance. Plans for public reporting in the near future. Sees implementation statements as an opportunity for member engagement.	Reports publicly against TCFD. Has an annual responsible investment update report for members.
Trustees keep abreast of industry discussions and attend events to improve knowledge and observe best practice. Considers becoming a signatory to the PRI.	Joins investor groups such as IIGCC. Engages with policy makers to improve practice across the industry.