Sackers

ESG and climate change for pension funds

A guide to trustee disclosures from 2021

Contents

Introduction

Download our previous ESG guides from our website.

Welcome to our latest guide for pension trustees on ESG investment and climate change.

We said in our 2020 guide that nothing stands still in the world of ESG, and that remains as true as ever in 2021. This will be our fifth guide for trustees, something we could never have imagined when our first guide was launched in 2016. This year, we have decided to focus on the disclosure aspects of ESG and climate change, reflecting the raft of new climate reporting obligations being introduced this year under the Pension Schemes Act 2021.

These new requirements are being phased in for larger schemes and master trusts first. They come hot on the heels of requirements introduced last year for schemes to produce annual implementation statements, with most schemes producing their first statements this spring/summer. The reporting deadlines for both implementation statements and climate reporting requirements will be dictated by scheme year ends, but operate slightly differently in each case. Getting your head around the various deadlines can be a little confusing, so on pages 4-5 we have set out a series of timelines for DB and DC schemes of different sizes and with scheme year ends of either 31 December or 31 March. On pages 6-9 we provide a recap on the SIP and implementation statement requirements. As usual though, trustees should confirm the deadlines and requirements applicable to their schemes with their advisers.

Climate change remains under the spotlight and should be a key focus for trustees this year. In our 2020 guide, we looked at how the consideration of climate-related issues should be part and parcel of trustees' fiduciary duties, but the law now goes further with mandatory disclosure requirements to be introduced from 1 October 2021. Warming to their theme, the DWP has said that meaningful disclosures on climate will not be possible without trustees undertaking certain governance activities, so for the first time the regulations tell trustees of schemes in scope not just what they must disclose on ESG matters, but also prescribe specific actions that must be taken first. This will be new ground for many and timing will be tight. On pages 10-17 we take a closer look at the new requirements and the key points trustees will need to consider.

For DB schemes, climate-related risks do not just stop at the scheme's assets. Sponsor covenant may be impacted too, so we are delighted to have our friends at Lincoln Pensions provide an overview of how trustees should approach this and, on pages 20-21, Michael Bushnell considers the disclosures trustees may require from their scheme sponsor.

In the rest of the guide, we look at other legal disclosure obligations trustees might find themselves subject to via member disputes or TPR involvement, the voluntary disclosures trustees might take on as PRI or Stewardship Code signatories, and finally what might be coming down the track for managers and other financial market participants from the FCA and the EU.

We hope you enjoy reading this guide. If you would like to discuss how your scheme can address any of the issues raised in this guide, please speak to any member of the Sackers team.

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ESG – your timeline for compliance

On these pages, we set out timelines for compliance with the various ESG and climate regulations. The timelines cover schemes of different types (DB, DC, hybrid) and sizes, with scheme year ends of either 31 December or 31 March. Schemes with different scheme years will require specifically tailored timelines – please speak to your usual Sackers contact to discuss further.

Schemes with a 1 January – 31 December scheme year end

	DB only schemes <£1bn	DB only schemes £1-5bn	DB only schemes >£5bn	DC / hybrid schemes <£1bn	DC / hybrid schemes £1-5bn	DC / hybrid schemes >£5bn	Master trusts all sizes
1 October 2019	Update SIP to include ESG and stewardship policies			Update SIP to include ESG and stewardship policies 🖱			
1 October 2020	Update SIP for SRDII to include policies on arrangements with asset managers 🖱			Update SIP for SRDII to include policies on arrangements with asset managers 🖱			
End of July 2021	Deadline for producing 1st implementation statement			Deadline for producing 1st implementation statement 🖱			
1 October 2021	Online publication requirement for 1st implementation statement 🖱						
			Climate governance requirements apply			Climate governance requirements apply	
31 December 2021			▨			▨	▨
End of July 2022	Deadline for producing 2nd implementation statement 🖱			Deadline for producing 2nd implementation statement 🖱			
			Deadline for producing TCFD report 🖱			Deadline for producing TCFD report 🖱	
1 October 2022		Climate governance requirements apply			Climate governance requirements apply		
31 December 2021		▨			▨		
End of July 2023		Deadline for producing TCFD report 🖱			Deadline for producing TCFD report 🖱		

🖱 Online publication requirement

▨ Complete climate governance activities required to be undertaken in first scheme year (eg scenario analysis)

Schemes with a 1 April – 31 March scheme year end

	DB only schemes <£1bn	DB only schemes £1-5bn	DB only schemes >£5bn	DC / hybrid schemes <£1bn	DC / hybrid schemes £1-5bn	DC / hybrid schemes >£5bn	Master trusts all sizes
1 October 2019	Update SIP to include ESG and stewardship policies			Update SIP to include ESG and stewardship policies			
1 October 2020	Update SIP for SRDII to include policies on arrangements with asset managers			Update SIP for SRDII to include policies on arrangements with asset managers			
End of September 2021	Deadline for producing 1st implementation statement (assumes completed report and accounts in 2020 prior to 1 October 2020)			Deadline for producing 1st implementation statement (assumes completed report and accounts in 2020 prior to 1 October 2020)			
1 October 2021	Online publication requirement for 1st implementation statement						
			Climate governance requirements apply			Climate governance requirements apply	
31 March 2022							
1 October 2022		Climate governance requirements apply			Climate governance requirements apply		
End of October 2022	Deadline for producing 2nd implementation statement			Deadline for producing 2nd implementation statement			
			Deadline for producing TCFD report			Deadline for producing TCFD report	
31 March 2023							
End of October 2023		Deadline for producing TCFD report			Deadline for producing TCFD report		

The climate governance requirements will be phased in with schemes with net assets (excluding bulk and individual annuity contracts) of £5bn or more and master trusts required to comply first from 1 October 2021.

Online publication requirement

Complete climate governance activities required to be undertaken in first scheme year (eg scenario analysis)

SIPs – a reminder

A SIP is a written statement governing decisions about investments for the purposes of an occupational pension scheme.

The SIP requirement was introduced in 1997 under s.35(3) of the Pensions Act 1995. Since then, a raft of additional requirements and recommendations have been implemented through different legislation.

Following the publication of the amended Investment Regulations in September 2018, trustees have faced a number of changes to the contents of their SIPs in respect of ESG. See our Alert.

From October 2019, trustees have been required to produce a clear policy on ESG, climate change and stewardship. This has been more than just finding the "right" words to put in a SIP. Careful thought is required on an ongoing basis as to how policies are integrated into trustees' portfolios and risk assessments.

Trustees should now be familiar with these new practices and have in place the appropriate systems in relation to preparing and updating the SIP.

Recap on SIP requirements

October 2019

Trustees were required to update or prepare their SIP, before 1 October 2019, to set out their policies in relation to "financially material considerations" (defined to include ESG considerations and climate change) over the appropriate time horizon of the investments, and their engagement activities in respect of investments (stewardship). SIPs also had to be updated to set out the extent (if at all) to which "non-financial matters" (generally member views on ethical matters) were taken into account.

Trustees of DC schemes also had to publish their SIP on a publicly available website.

October 2020

Further changes to the Investment Regulations were made in 2019 to implement aspects of SRD II in the UK. These required trustees to make further changes to their SIPs by 1 October 2020, setting out the following in relation to their arrangements with their asset managers (or explaining why they are not set out):

- how asset managers are incentivised to align their investment strategy and decisions with the trustees' investment policies, including in relation to ESG matters
- how asset managers are incentivised to make decisions based on assessments about medium-to-long-term financial and non-financial performance of an issuer of debt or equity, and to engage with issuers of debt or equity in order to improve their performance over that term
- how the method (and time horizon) of the evaluation of the asset manager's performance and the remuneration for asset management services are in line with the trustees' investment policies
- how the trustees monitor portfolio turnover costs incurred by asset managers, and how they define and monitor targeted portfolio turnover or turnover range, and
- the duration of the arrangement with the asset manager.

The methods by which trustees monitor and engage with investee companies and other stakeholders in relation to their capital structure, and the management of conflicts of interest, were also required to be set out.

A public document means public scrutiny

The requirement for SIPs and implementation statements (see pages 8-9) to be made available online will, for many schemes, increase the likelihood of public scrutiny:

- in December 2019, ShareAction used publicly available SIPs to publish a review of UK master trusts' ESG policies, grading each master trust on its performance (see our guide "ESG and climate change for pension funds: Your agenda for 2020")
- in February 2020, UKSIF published their report on pension scheme compliance with the new SIP requirements
- in August 2020, the DWP consultation "Taking action on climate risk: improving governance and reporting by occupational pension schemes" stated that: "Research suggested that advised pension scheme trustees are complying with the letter of the law [regarding SIPs] but taking their time to make decisive changes to strategy".

Trustees should assume these documents will be read not just by their members but by other organisations which may seek to hold trustees accountable for their actions (or inaction).

In addition, regulations under the Pension Schemes Act 2021 requiring TPR to collect the website addresses of schemes' SIPs via the annual scheme return are due to come into force on 1 October 2021. TPR has said that it will begin to publish the SIP website addresses when they are collected in subsequent scheme returns and "will be working on the creation of an index of SIPs, which will help us check for breaches of compliance with disclosure regulations."

Tips and reminders for updating your SIP

1

Allocate time within a trustee or investment sub-committee meeting to consider the trustees' overall approach. What policies can realistically be adopted based on overall investment strategy and governance budget, as well as the nature of the scheme's investments?

2

Where ESG issues and stewardship are delegated, ensure manager policies and mandates are consistent with the trustee policies stated in the SIP. In the context of segregated mandates, consider whether to request any change to investment objectives, restrictions and reporting requirements to reflect policies stated in the SIP.

3

Consider whether a standalone responsible investment policy may be a better approach than seeking to put everything in the SIP. This can be a helpful tool to explain the trustees' approach to members in a more accessible format and can be a useful way of keeping the SIP in shorter form.

4

Write the SIP with the implementation statement in mind. For relevant schemes (broadly, schemes providing DC benefits other than AVCs), all policies under the SIP are in scope for the implementation statement, so trustees should take care not to include general statements in their SIPs which may be hard to report against.

Implementation statements – where are we now?

From 1 October 2020, trustees were required to produce an implementation statement setting out how they acted on the policies set out in the SIP. The timing and content requirements of the implementation statement are not entirely straightforward in the Disclosure Regulations and apply differently to schemes based on their scheme year (see our timeline on pages 4-5 for further details). Trustees should take advice on this from their usual advisers as the precise timing and content will vary for each scheme.

The key points

- All schemes must prepare their implementation statement for inclusion in their first annual report and accounts produced after 1 October 2020. As trustees are required to prepare this within seven months of the end of each scheme year, a scheme with a 31 December year end will have until July 2021 to prepare their first implementation statement. Schemes with a 31 March year end had a choice of producing their first implementation statement in October 2020 (if they used the full seven months to prepare their annual report and accounts for the 2019-2020 scheme year), or wait until October 2021 if they completed that year's report and accounts within six months (ie before 1 October 2020). Trustees should ensure that they take advice on how the deadlines apply to their scheme.
- The requirements in relation to the content of the annual report and accounts are included in the Disclosure Regulations.
- For pure DB schemes, the content is generally limited to a report on the engagement activities and votes exercised during the year.
- For DC schemes (and schemes which provide both DB and DC benefits), the content requirements are more extensive, and trustees will need to report generally on the implementation of their ESG and other policies across the scheme (including in relation to any DC default fund) as well as their engagement activities and voting.

The requirements do not apply to schemes with fewer than 100 members.

Practical tips and guidance

1

TPR's DC investment guidance explains that the statement's purpose is to help ensure that "action follows intent" as far as possible. The process of having to consider the content of the statement is intended to help to "focus trustees' minds on how well their investment policies and stewardship arrangements are delivering against their scheme's agreed investment principles".

2

Guidance published by the PLSA includes some suggested high-level "general principles" for implementation statements, as well as "top tips" for responsible investment communication. Trustees drafting their statements for the first time should consider the PLSA guidance essential reading.

Required content	DB-only schemes	Relevant schemes (DC and hybrid)
Set out how, and the extent to which, the scheme's policies on stewardship from the SIP have been followed during the scheme year	✓	✓
Set out how, and the extent to which, the SIP has been followed during the scheme year	✗	✓
Describe any formal review of the SIP (as required by the Investment Regulations) undertaken during the year, and any other review of how the SIP has been met	✗	✓
Explain any change made to the SIP during the scheme year and the reason for the change	✗	✓
Where no formal review was undertaken during the scheme year, provide the date of the last review	✗	✓
Describe the voting behaviour by, or on behalf of, the trustees (including the most significant votes cast by the trustees or on their behalf) during the scheme year, stating any use of the services of a proxy voter	✓	✓

Online publication

As well as including the implementation statement in the annual report and accounts, trustees must also make it publicly available online (see timeline on pages 4-5).

3

At present, the FCA requires asset managers to produce a "general description" of their voting and engagement behaviour – likely to happen at a firmwide level. However, trustee boards need to report their voting behaviour at a scheme level, which will require mandate-level or fund-level information. The PLSA has produced a vote reporting template and accompanying guidance to help trustees and asset managers disclose how they enact their shareholder voting rights. The publication of the voting template is intended to promote consistent and uniform reporting of information.

4

Consider keeping a record of investment policy implementation and actions as you go along. Keeping an investment implementation log of key events (such as asset manager reviews) through the year will make it easier to prepare the statement when due. The PLSA guide provides examples of key actions or decisions, taken over the course of the scheme year, which trustees might choose to report.

Climate-related disclosures – an introduction

All pension schemes are exposed to climate-related issues. In making investment decisions, trustees should consider all relevant factors which are financially material and act prudently. In our fourth ESG guide, we set out the arguments for trustees to consider climate-related risks and opportunities from a fiduciary and trusts law perspective.

In its Green Finance Strategy, published in July 2019, the Government set out its expectation for all listed companies and large asset owners to make climate-related disclosures in line with recommendations made by the TCFD. Making good on this expectation, the Pension Schemes Act 2021 provides a regulation-making power that can be used to mandate such reporting by pension schemes, requiring trustees to carry out associated governance actions.

On the 8 June 2021, the DWP published its response to its January consultation "Taking action on climate risk: improving governance and reporting by Occupational Pension Schemes" (see our Alert) together with revised draft regulations and draft statutory guidance. The final regulations were approved by parliament in July 2021 and are due to come into force on 1 October 2021, with larger schemes being the first to comply[1]. To help trustees do this, and consider what actions would be appropriate in their own scheme's circumstances, the PCRIG has published guidance for trustees on the integration of climate risk into decision-making. Sackers is proud to have led the development of this cross-industry guidance. In addition, on 5 July 2021, TPR published its own consultation on its approach to the new regulations and proposed guidance for trustees.

Using the TCFD recommendations

Published in 2017, the TCFD's recommendations establish a set of 11 clear, comparable and consistent disclosures through which exposure to climate-related financial risks and opportunities can be identified, assessed, managed and disclosed.

The TCFD recommendations can be considered in four areas, as applicable, to pension trustees as follows:

Governance – disclose the trustees' governance procedures around climate-related risks and opportunities

Strategy – disclose the actual and potential impacts of climate-related risks and opportunities on the pension scheme where that information is material

Risk Management – disclose how the trustees identify, assess, and manage climate-related risks

Metrics and targets – disclose the metrics and targets the trustees use to assess and manage climate-related risks and opportunities where that information is material.

Although the TCFD recommendations focus on "disclosures" by organisations, the framework is fundamentally a useful tool for pension trustees in assessing the relevance of climate change and managing any consequences. The TCFD recommendations form the basis of the regulations and accompanying statutory guidance published in June 2021. Over the following pages 11–17, we set out the requirements in further detail.

1 For the timings and scope of the regulations see pages 4-5

TCFD
Governance

Requirements under the regulations

Trustees of schemes in scope must establish and maintain, on an ongoing basis, oversight of the climate-related risks and opportunities which are relevant to the scheme.

They must also establish and maintain processes for the purpose of satisfying themselves that persons undertaking governance activities on their behalf are taking adequate steps to identify, assess and manage any climate-related risks and opportunities which are relevant to the governance activities they are undertaking, and that persons who advise or assist the trustees with respect to governance activities are taking adequate steps to identify and assess climate-related risks and opportunities.

TKU

Trustees must have an appropriate degree of knowledge and understanding of the principles relating to the identification, assessment and management of climate change risks and opportunities in respect of occupational pension schemes

The first step in implementing TCFD recommendations is for trustees to make sure climate-related risks and opportunities are integral to their usual governance procedures. Not only should this make it easier to comply with disclosure requirements when they begin to bite, but it will help to provide a sound framework around which investment decisions can be made.

On 17 March 2021, TPR launched a consultation on the first part of its new combined code of practice, making clear its expectations that trustees of all schemes should be considering climate-related risks and opportunities, and specifically that trustees of any scheme with 100 members or more are expected to:

- maintain and document processes for identifying and assessing climate-related risks and opportunities, and
- integrate these processes into their risk management and governance arrangements.

Key points to consider

- Trustees' investment beliefs in relation to climate-related issues should be codified in current documents (such as the scheme's SIP) with further detail set out within any trustee ESG or climate policy.
- Trustees should allow appropriate time and ongoing training to ensure that they have a sufficient understanding of climate issues.
- Trustees should consider the roles and responsibilities within the trustee board (and, where applicable, any sub-committees and/or individuals/organisations providing executive support to the trustees) for climate-related issues.
- Trustees should consider how their process for the selection, review and monitoring of the scheme's asset managers takes account of climate change issues.
- In practice, many trustees will rely heavily on their advisers and consultants to provide, identify and/or assess climate-related risks and opportunities, and to provide strategic advice about investment strategies, asset allocation and asset manager selection. The Investment Consultants Sustainability Working Group ("ICSWG") have produced a helpful "Guide for assessing climate competency of Investment Consultants". When using external advisers, trustees should consider and document the extent to which these responsibilities are included in any agreements, such as investment consultants' strategic objectives and service agreements.

TCFD
Strategy

Requirements under the regulations

- Trustees of schemes in scope must identify the climate-related risks and opportunities which they consider will have an effect on the scheme's investment strategy (and funding strategy where applicable) and assess their impact.
- Trustees are required to identify these risks and opportunities and their impact over the short, medium and long term.

Considering climate change as part of a scheme strategy will involve considering how climate-related issues might impact the scheme's investment portfolios (including the default fund(s) in a DC scheme) and, in a DB scheme, its funding strategy and employer covenant.

When thinking about their investments, trustees should consider how they intend to factor climate-related risks and opportunities into the scheme's investment strategies – both at total fund/strategy level, and individual asset class level. Of course, pension fund investment allocations are unlikely to stand still. In a DB scheme, they may be expected to change over time with a derisking flight plan and, in a DC scheme, they may be expected to change as part of a lifestyling plan. Trustees will need to take care to identify and take into account within their consideration of strategy any areas where asset allocation ranges and portfolio structure are expected to evolve in the future.

Key points to consider

- Trustees are required to disclose in their TCFD report the time periods they have chosen for the short, medium and long term. The regulations define these as the time periods which the trustees determine are appropriate "taking into account the scheme's liabilities and its obligations to pay benefits". The PCRIG guide suggests that, in DB schemes, the longest time horizon to be considered will be the time over which the benefits will be paid to their members from the scheme. In DC schemes, the longest time horizon to be considered will be the time over which members' money will be invested via the scheme.
- When implementing a scheme's investment strategy, it is vital that asset managers are assessed on the extent to which they address climate risk and take advantage of related opportunities. The PCRIG guidance sets out the key queries that should be raised with asset managers to make sure climate change is on their agenda.
- Amendments to the Investment Regulations, which took effect from October 2019, required all schemes to have a stewardship policy but, in many cases, these will state that the trustees delegate stewardship activities to the scheme's asset managers. Where this is the case, trustees should familiarise themselves with the managers' stewardship policies in relation to climate-related issues, ensure that these are in line with the trustees' climate-related investment beliefs, and hold their managers to account in relation to their engagement activities and voting record on climate issues.
- For DB schemes, there are additional strategic issues to consider. Climate change could impact not only the assets held but the covenant of the scheme's sponsoring employer. Particular thought should be given to this where a sponsor is part of a high-carbon industry, or where there are parts of their business that are vulnerable to extreme weather or changing climate. Any covenant advice taken should demonstrate an understanding of these risks and their materiality to the scheme's long-term strategy.

TCFD
Scenario analysis

Requirements under the regulations

Trustees of schemes in scope must, as far as they are able, undertake scenario analysis assessing the impact on the scheme's assets and liabilities, the resilience of the scheme's investment strategy and (where it has one) the scheme's funding strategy for at least two scenarios – one of which corresponds to a global average temperature rise of between 1.5 and 2°C inclusive on pre-industrial levels.

Scenario analysis must be carried out in the first year in which the requirements apply to the scheme, and at least every three years thereafter. Whenever trustees undertake fresh scenario analysis, the triennial cycle is automatically reset. Where a scheme has both DB and DC sections, separate scenario analysis will be required for both the DB section(s) and the DC default fund(s).

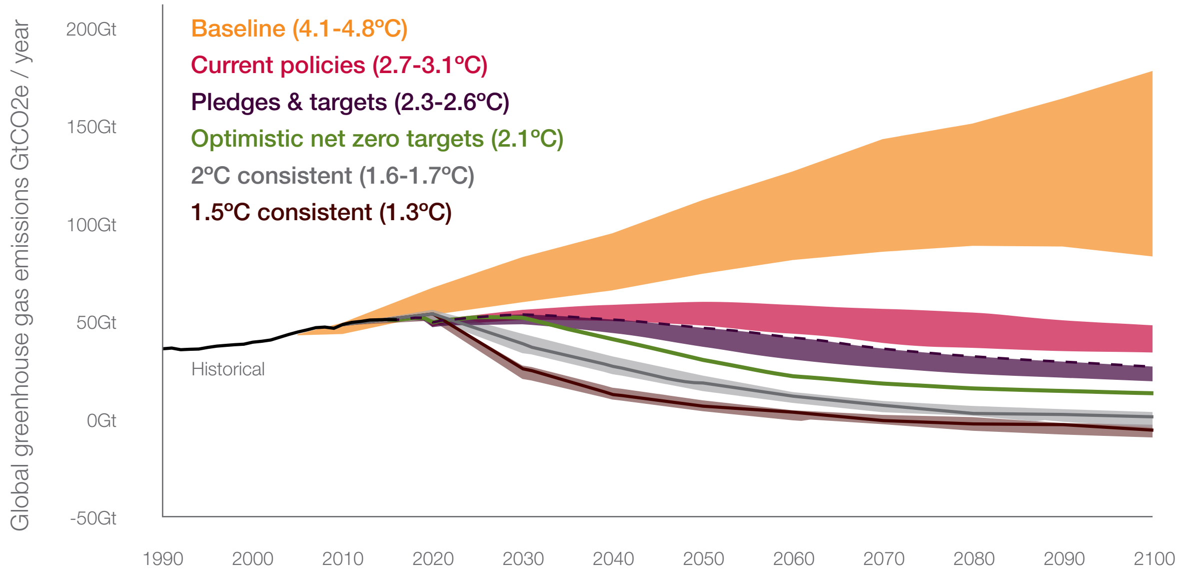
Scenario analysis is a well-established tool for understanding possible alternative futures and developing strategic plans that are more flexible or robust to a range of plausible future states. Pension schemes can use scenario analysis to assess their scheme's resilience to climate-related risks and opportunities, including:

- asset-side changes such as potential earnings impairment or enhancement of companies in which they invest and to whom they lend – for example, as a result of transition policies, demand changes, physical impacts, and other factors such as litigation risks
- in the case of DB schemes, liability-side changes such as inflation, interest rates, longevity and the strength of the sponsoring employer covenant.

Carrying out climate scenario analysis is a key element of the new regulations and a required element of reporting for schemes in scope.

2100 Emissions and Warming Projections

Emissions and expected warming based on pledges and current policies



Source: Climate Action Tracker, Dec 2020 update

Key points to consider

- For schemes in scope, scenario analysis must be undertaken in the first scheme year in which the regulations apply. For schemes with a 31 December year end, this might mean that scenario analysis has to be carried out within three months of the regulations applying and, for schemes with a 31 March year end, within six months. Trustees should ensure that they can carry out the required analysis by the deadline applying to their scheme, identifying early on who is going to conduct the scenario analysis and ensuring that the trustees allow sufficient time for training to understand the models they will be using.
- Scenario analysis must be undertaken for each "sectionalised" section in a DB scheme (unless those sections have sufficiently similar characteristics in relation to assets, liabilities and funding) and for each "popular" arrangement in a DC scheme[2]. Large or complex schemes may therefore find that they need to carry out several different scenario analyses.
- The statutory guidance also sets clear expectations that DB scheme analysis will need to cover, not only the scheme assets, but also the sponsor covenant and the potential implications of different climate scenarios on actuarial assumptions and funding. This may be new ground for many trustees and, again, emphasises the need for trustees to get ahead of the game, taking advice from their actuarial and covenant advisers. Trustees may prefer to carry out "qualitative" as opposed to "quantitative" analysis on funding and covenant matters.
- The regulations require trustees' scenario analysis to include at least two climate scenarios – one of which corresponds to a below 2°C temperature rise consistent with the Paris Agreement and one above. However, the route by which a below 2°C temperature rise may be achieved may be dramatically different where the world's economies (and regulation) transition in an orderly manner to the required low carbon future, as opposed to where regulation and changes in behaviours are left late before a sudden and disorderly tightening of policy as countries rush to get on track with the Paris Agreement. Trustees may, therefore, wish to consider modelling three climate scenarios consistent with the recommendations in the PCRIG guide: (1) orderly transition, 1.5-2°C scenario; (2) an abrupt transition, 1.5-2°C scenario; (3) no transition, pathway to 4+°C scenario.
- Climate scenario analysis is inevitably subject to limitations due to the difficulties of modelling such a complex phenomenon as climate change. Trustees may wish to use scenario analysis to illustrate possibilities and help them make climate-informed investment (and for DB schemes funding decisions) but should bear in mind that scenario models are not forecasts or predictions.
- Trustees are not required to disclose the entirety of their scenario analysis as part of their TCFD reporting. Consideration should be given to how much might usefully be reported.

2 Statutory guidance provides that a "popular" arrangement is one in which £100m or more of the scheme's assets are invested, or which accounts for 10% or more of the assets used to provide money purchase benefits (including assets which are solely attributable to AVCs)

TCFD
Risk management

Requirements under the regulations

- Trustees of schemes in scope must establish and maintain, on an ongoing basis, processes for identifying, assessing and effectively managing climate-related risks which are relevant to the scheme and integrate them into the trustees' overall risk management of the scheme.
- They should then describe the processes they have established in their TCFD report and how these are integrated within the overall risk management of the scheme.

Trustees should always take into account any relevant matters which are financially material to their investment decision making. This may well be about whether a particular factor is likely to contribute positively or negatively to anticipated returns. But, it may equally be about whether a factor will increase or reduce risk. That climate change might pose a significant financial risk to pension schemes is becoming increasingly apparent and, where financially material to a scheme, it should be taken into account by trustees in their investment decision making[3].

The statutory guidance makes clear that trustees must adopt and maintain processes for the purpose of enabling them to identify and assess climate-related risks which are relevant to the scheme.

Types of climate-related risks

When considering the financial implications of climate change, a distinction can be drawn between **transition risks** and **physical risks**. The former relate to the risks (and opportunities) from the realignment of the economic system towards low-carbon, climate-resilient or carbon-positive solutions (eg via regulations or market forces). The latter relate to the physical impacts of climate change (eg rising temperatures, rising sea levels, and increased frequency and severity of extreme weather events).

Key points to consider

- Trustees should revisit their risk registers and add climate-related risks as a consideration. Trustees should consider risks to both the scheme's investments and, in the case of DB schemes, funding and sponsor covenant. The statutory guidance suggests that processes for assessing risks should be applied at the asset-class or key sector level as a minimum.
- Trustees may rely on other persons, including advisers and asset managers, to help them identify and assess climate-related risks. However, as the statutory guidance makes clear, trustees have overall responsibility for the management of these risks. Paragraph 100 of the statutory guidance sets out a number of possible approaches to identifying and assessing transition risks and physical risks.
- As discussed in TPR's Integrated Risk Management guidance, risk identification should not be a one-off exercise. Trustees will need to consider how often they revisit their assessment of climate-related risks and the processes for doing so and staying on top of developments.

3 Keith Bryant QC and James Rickards, The legal duties of pension fund trustees in relation to climate change (November 2016)

TCFD
Metrics and targets

Requirements under the regulations

- Trustees of schemes in scope must select and report on at least three climate-related metrics for each of a scheme's DB sections and popular DC arrangements[4] as follows:
  - one "absolute emissions" metric – the statutory guidance recommends total GHG emissions of the portfolio
  - one "emissions intensity" metric – the statutory guidance recommends tonnes of GHG emissions for each million (£m) of the scheme's assets
  - one "additional" climate change metric – the statutory guidance provides a range of options (see below).
- Trustees will be required, "as far as they are able", to use total emissions and carbon footprint metrics – calculating Scope 1 and 2 GHG emissions in the first scheme year they are subject to the requirements, and then Scope 1, 2 and 3 in all subsequent years (see further below).
- If trustees use a different absolute emissions or emissions metrics from those in the statutory guidance, they should explain why.
- Trustees must set a non-binding target for the scheme in relation to at least one of their chosen metrics and, as far as they are able, measure performance against it on an annual basis.

Disclosing emissions and other climate-related metrics is a key element of the new regulations and, rightly or wrongly, trustees should not be surprised if members and civil society groups use a scheme's disclosures as a yardstick to judge their climate performance.

For their emissions metrics trustees will need to understand the distinction between an issuer's direct GHG emissions (Scope 1 and 2) and indirect GHG emissions (Scope 3):

- scope 1 – all direct emissions from the activities of an organisation or under their control, including fuel combustion
- scope 2 – indirect emissions from electricity purchased and used by the organisation. Emissions are created during the production of the energy which is eventually used by the organisation
- scope 3 – all other indirect emissions from activities of the organisation, occurring from sources that they do not directly control, including supply-chain operations and end-product usage by customers. For some companies and industries, Scope 3 emissions dominate the overall carbon footprint.

For their "additional" climate change metric, the statutory guidance provides three examples of non-emissions metrics which trustees might use[5]. These are:

- a portfolio alignment metric – for example a "degree warming metric", which shows a potential global temperature rise associated with the GHG emissions from a given company or portfolio
- climate value at risk (VaR) – expressed as a potential loss, at a certain level of probability over a relevant timeframe – for example, a potential loss of 20% by 2030 at a 90th percentile for an eventual below degrees scenario
- data quality – this measure aims to represent the proportions of the portfolio for which the trustees have high quality data.

4 See footnote 2 above

5 The regulations describe the "additional" metric as any metric of the trustees' choosing which does not meet the definition of the two required emissions-based metrics in the regulations. However, at the time of writing, the statutory guidance is not clear that trustees have a greater choice than the three additional metrics indicated in the guidance. It is hoped that this will be clarified following consultation, to make clear that trustees have flexibility to select an additional metric that best suits the circumstances of their scheme

Key points to consider

- Whilst emissions-based metrics provide some visibility into the past carbon exposure of assets at a fixed point in time, they may provide little insight into potential future exposure. Trustees may wish to consider the limitations and backward-looking nature of such metrics, particularly when considering options for their "additional" metric and which metric(s) they intend to set targets for.
- Trustees are only required to calculate one emissions intensity metric. However, the statutory guidance states that they may, if they wish to, additionally report the Weighted Average Carbon Intensity ("WACI") (in tCO_2e / £m) of their portfolio. In our experience, many trustees who have already considered climate metrics may have a preference for WACI rather than absolute emissions metrics. Trustees should assess their preferred emissions-based metric, and may need to consider carefully how an array of different emissions metrics will be presented in their reporting without causing confusion.
- Currently, the state of Scope 3 reporting is poor, with corporate reporting frequently incomplete and at times highly volatile. There is also a risk of double counting the Scope 3 emissions of one organisation as Scope 1 emissions of another. Trustees will need to understand assumptions made or models used by parties providing data to them. The statutory guidance provides that trustees should set out the Scope 1 and 2 emissions of assets separately from the Scope 3 emissions.
- The requirement for trustees to obtain data "as far as they are able" will be a key issue for trustees to consider. The regulations define this as trustees taking all such steps as are reasonable and proportionate in the particular circumstances, taking into account the costs, or likely costs, which will be incurred by the scheme, and the time required to be spent by the trustees or any people acting on their behalf. The statutory guidance provides that trustees must also explain any missing data and, where there are significant gaps, consider seeking alternate third party sources of data or modelling to fill them, explaining any modelling/assumptions in their reporting. This will be a key decision point for trustees. Trustees should make enquiries of their managers as soon as possible to identify what metrics they are capable of supporting (in particular, their capacity to report Scope 3 emissions data). Where trustees are reliant on their asset managers to provide data, they may also need to consider whether it will be reported with sufficient consistency to enable the trustees to aggregate data across their portfolios.
- Finally, trustees should take care not to get carried away with metrics and target setting for its own sake. Metrics chosen should be those which help trustees make informed decisions about financial risks and opportunities in their portfolios. Targets should be set to support the trustees' fiduciary and trusts law duties to pay members' pensions, rather than to deliver on external outcomes for society at an increased cost or risk to the pension scheme. Trustees will need to keep this in mind when making their decisions about which metrics are most useful/appropriate for their own scheme and when identifying any targets.

Member queries and disputes

For trustees grappling with their statutory disclosure obligations in relation to climate change and ESG issues more generally, it is important to know that they are not the only disclosure obligations that might apply.

Other information disclosure obligations

The Disclosure Regulations set out additional information that must be provided to members, both automatically and upon request. The former consists largely of what is described as "basic scheme information". The latter includes the trust deed and rules, the scheme's annual report, and the latest SIP.

In addition, under case law, a beneficiary may be entitled to other documentation held by trustees. Although there is some debate as to what exactly it requires, in practice trustees should consider all the circumstances of the request and balance any competing factors for and against disclosure, particularly when there are issues as to personal or commercial confidentiality.

And finally, there are specific rules that apply regarding the disclosure of relevant documentation in the context of a member complaint to the Pensions Ombudsman, or court proceedings.

A beneficiary's entitlement to scheme documentation – the case law

This case law was tested in a climate change context through a complaint by a member (known as "Mr D", supported by ClientEarth) to the Pensions Ombudsman that was decided in August 2019.

Mr D requested, and was provided with, a copy of the scheme's latest actuarial valuation, its SIP, and its responsible ownership policy. The trustees also offered to, and did, meet with Mr D to discuss his concerns around climate change and the threat that it posed.

But Mr D was not satisfied and also requested a copy of the scheme's recent investment strategy, including sections that specifically dealt with climate change, and any minutes of trustee meetings in the last two years recording decisions the trustees had made in relation to climate change.

These additional requests were refused, citing a number of factors including confidentiality and commercial sensitivity of the information, the relevance of the additional documents to Mr D's personal benefits, resourcing requirements, proportionality and potential conflicts of interest.

Mr D argued that the trustees' refusal to provide requested information relating to climate change risks amounted to maladministration. However, the Deputy Pensions Ombudsman held that there was no breach of a positive disclosure duty, either under case law or legislation, nor was there maladministration in declining the member's requests.

Of course, it should be noted that the case preceded the new climate disclosure requirements coming into force this year, so trustees should be cautious in applying the decision too rigidly to their own approach to member engagement.

Disclosure in legal proceedings – a back-door route?

The increased legal obligations on trustees in relation to ESG issues elevate the risk of non-compliance or, at least, alleged non-compliance. And this may give a basis for obtaining the disclosure of information through the back door of any legal proceedings where non-compliance is alleged. This was seen recently in the context of climate change with the Australian case of McVeigh.

There, the court proceedings were brought by a member with funding support from Friends of the Earth. Initially, the member simply alleged that the DC pension scheme (in Australia, known as a superannuation fund) was required by statute to tell the member more than it had about the steps it was taking to address the financial risks posed to his benefits by climate change.

Subsequently, the member changed his claim also to allege that the trustee had breached its legal duties by not having a more developed climate change policy than it had indicated. This resulted in the judge himself speculating that at least part of the reason for the claim was to put pressure on the trustee to defend itself, by disclosing more information about what it had done in relation to climate change than it had up until that point.

Whether for that reason or another, we do not know, a confidential settlement was reached in November 2020. This included a public commitment from the trustee to implement a long-term objective to achieve a net zero carbon footprint for the fund by 2050, and to implement changes to its climate change policy and internal risk framework. We also do not know whether the settlement involved providing the member with some or all of the information he was seeking. But, this may be a route we also see tested by a member in the High Court in the not too distant future.

Disclosure to TPR

Of course, members may not be the only ones who are interested in knowing more about trustees' conduct. Responsible for enforcing compliance, TPR has a dedicated investigations team that has an array of tools at its disposal to obtain information. These include the ability to require the disclosure of any documents relevant to the possible exercise of its functions, as well as the ability to compel attendance at an interview.

Although TPR is bound by certain confidentiality restrictions, it is able to publish reports into the exercise of its functions in any particular case and these reports may include information obtained by TPR through its investigation. When deciding whether to publish, TPR has regard to its aims of transparency, education and guidance, as well as deterrence.

Coupled with TPR's widely anticipated "climate change strategy", we may see TPR taking a more aggressive role in driving trustee action on the risks and opportunities from climate change.

> TPR's information gathering tools include receiving "breach of law reports" (commonly known as whistle-blowing) and requiring the compulsory disclosure of documentation. Under the Pension Schemes Act 2021, TPR will also be able to compel attendance at an interview to answer questions in relation to the exercise of its functions.

Legal professional privilege

The Pensions Ombudsman, the courts, and TPR are all precluded from requiring the disclosure of documentation that is covered by legal professional privilege. TPR's interview powers are similarly restricted. While this is a complex area, trustees should be alive to the possibility of appropriate reliance on legal professional privilege in these circumstances, and consider in advance how it might operate.

What does this mean for the future?

Climate change and ESG issues more generally are only likely to become more prominent in the pensions landscape, and trustees' actions (or inaction) will become subject to greater scrutiny. How trustees choose to respond to this will vary. But having a good grip of their legal obligations will be an important starting point to deciding whether to go further and, if so, how.

Climate disclosures – interaction with DB scheme sponsors

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Climate change, and the world's response to it, is expected to have a fundamental impact on sponsors, with most, if not all, exposed to climate-related risk in some form.

However, despite the eminent risks, the impact on the employer covenant that could occur due to climate change is often not considered in detail by trustees or sponsors, potentially due to:

- a lack of accessible information, which can make it difficult to grasp
- the complexity of the issue, which can make it daunting
- prioritisation of challenges that seem more immediately "at-hand" to trustees or have historically had a higher level of focus in regulation.

All change

Increasingly, trustees and sponsors are coming to realise that the employer covenant should not be ignored when looking at the impact of climate change on a scheme. This change in approach is in line with regulatory pressure and specific requirements under the Occupational Pension Schemes (Climate Change Governance and Reporting) Regulations 2021.

It is clear that at some stage trustees will need to consider the climate exposure of their scheme sponsor, and to do so will require a whole new set of information and learnings; however, the tools may already be familiar to many trustees.

Painting an (internally-consistent) picture

Scenario analysis is a key tool for trustees when looking at the exposure of the employer covenant to the risks of climate change. Internally-consistent, plausible scenarios that can be applied across different elements of a scheme allow trustees to simplify the issues at hand and explore possible risks. A scenario-based approach has been highlighted by regulatory bodies including the DWP, Bank of England and others.

Whilst still useful, there are potential pitfalls with relying solely on other approaches. For example, stochastic models of climate outcomes tend to be too complex and too exposed to modelling errors to be reliable in the case of a single sponsor. In addition, new wave ESG ratings prepared for investment managers are not yet consistent in their approach, and their bespoke methodologies mean the outputs cannot be easily integrated with actuarial and investment analysis.

Good scenario analysis should ideally have a number of elements:

- Consideration of a range of scenarios that draw out both "transition risks" (greater in a low-warming scenario) and "physical risks" (greater in a high-warming scenario)
- Assumptions and variables that can be applied (broadly consistently) to covenant, investment and actuarial advice, with a level of transparency that allows trustees to interrogate the analysis
- Identification of a sponsor's operations, climate footprint, markets, supply chain and future plans
- Clear conclusions and recommendations on how the scheme might manage highlighted risks

Orderly transition, 2°C or lower scenario – emission reductions start now and continue in line with the Paris Agreement

1

Significant transition risks, lower physical risks

Abrupt transition, 2°C or lower scenario – little climate action in short term, followed by sudden unanticipated tightening as countries rush to get on track

2

Severe transition risks, lower physical risks

No transition, pathway to 4+°C scenario – continuation of historic emission trends and failure to transition away from fossil fuels

3

No transition, severe physical risks

The range of scenarios chosen may vary from scheme to scheme to ensure that the most crucial issues are brought out, but a sensible starting point in many cases will be the recommendations of the PCRIG, as shown to the left.

Information "makes the world go 'round"

Accurate information is a critical factor in effectively understanding the impact of climate change on a sponsor. The needs of a trustee are likely to be high, but the good news is that a lot of the information is likely to be available already.

Much public information can be sourced from a sponsor's existing reporting:

- company annual accounts will detail the basic financial information required and may give a guide to locations, staffing and operations, and voluntary or mandatory reporting on climate risks (in line with TCFD recommendations and including GHG emissions metrics) should also be included in accounts
- company public announcements increasingly focus on sustainability aims and can be a valuable guide to future plans
- sponsor websites can help highlight key locations or products
- significant information on industry risks are available in the public domain
- sponsors often have to assess and report their exposure to climate risks under government or regulatory requirements.

While public domain information might allow trustees to begin to build an understanding of the exposure of their employer covenant to the risks of climate change, engagement with a sponsor will provide trustees with better tailored and more accurate information and, therefore, conclusions. It is also likely to be beneficial to a sponsor; many sponsors may not have prepared formal analysis of these risks, or may appreciate the opportunity to demonstrate the mitigation plans they have in place.

There are some common pitfalls in gathering information that trustees will need to avoid:

- information should be relevant to a scheme's employer covenant and not just provided on a "group-wide" basis, where possible
- in preparing the analysis, confidential sponsor information may be received and should be handled appropriately; a non-disclosure agreement with trustees and advisors may be helpful, as in a corporate transaction
- in practice, the desired information may not be available and approximations may have to be made; scenario analysis should be flexible enough to cope with this and still provide useful conclusions.

Finally, as well as information on the sponsor, trustees will need either to understand the potential impact of climate change and associated legislation, or to seek help from advisors on these issues. A detailed study of the issues could take a lifetime but much helpful information is already in the public domain[6].

Employer covenant has long been the missing piece of the sustainability jigsaw but increasingly, with regulatory input, trustee perseverance and advisor support, that is changing for the better.

6 https://unfccc.int/
https://www.tcfdhub.org/
https://www.unpri.org/

Voluntary codes – PRI and stewardship

In addition to regulatory requirements, there have for a number of years been independent and voluntary codes which allow pension scheme trustees to adopt widely recognised industry standards. For schemes looking to demonstrate that they take responsible investment matters seriously, signing up to voluntary codes is attractive as they provide a framework of ready-made principles.

For convenience, we set out below a brief description of two of the codes trustees (and their managers) may be most likely to engage with.

PRI

The Principles for Responsible Investment ("PRI") are a voluntary and "aspirational" set of principles aimed at asset owners, managers and service providers. The PRI were developed by an international group of institutional investors in a process convened by the United Nations Secretary-General. The PRI are based on a core belief that institutional investors have a duty to act in the best long-term interests of their beneficiaries and that ESG issues can affect the performance of investment portfolios (to varying degrees across companies, sectors, regions, asset classes and through time). In our experience, this is well aligned with most pension scheme trustees' existing beliefs.

Principle		
	1	We will incorporate ESG issues into investment analysis and decision-making processes
	2	We will be active owners and incorporate ESG issues into our ownership policies and practices
	3	We will seek appropriate disclosure on ESG issues by the entities in which we invest
	4	We will promote acceptance and implementation of the Principles within the investment industry
	5	We will work together to enhance our effectiveness in implementing the Principles
	6	We will each report on our activities and progress towards implementing the Principles

In 2018, the PRI implemented minimum requirements for PRI signatories, stating that pre-existing and future signatories who fail to meet these requirements over a two-year period, following extensive engagement with the PRI, will be delisted.

Since 2018, it has been compulsory for PRI signatories to report on their responsible investment activities annually. Trustees preparing for the 2021 reporting cycle should avail themselves of the PRI's investor reporting guidance.

The PRI reporting framework includes:

- questions relating to the organisational overview of the trustees
- indicators relating to the trustees' overall approach to ESG incorporation, stewardship policy and TCFD questions
- asset class specific modules, each having a set structure and following key elements of ESG incorporation
- voluntary reporting on sustainability outcomes.

FRC's UK Stewardship Code 2020

The Financial Reporting Council's ("FRC") UK Stewardship Code 2020 ("the Code") sets outs high stewardship standards aimed at those responsible for investing the assets of UK savers and pensioners, and those who support them.

Signatory organisations are required to apply all relevant principles in the previous 12 months and compliance is now monitored on an "apply and explain" approach through an annual reporting process. The FRC will evaluate reports submitted and only those that meet its expectations will be listed as signatories to the Code. This was a significant shift from the Stewardship Code 2012, and a response to a perception that some institutional investors were signing up to that code but taking very little action to implement it. Once a signatory's report is approved by the FRC, the report will be a public document and must be made available on the signatory's website.

To be included in the first list of signatories, trustees must submit a **final** report to the FRC by 30 April 2021 covering the period 1 January 2020 – 31 December 2020. More information about the submission process and how to apply is available on the FRC's website.

Standards	Principle
Purpose and governance	Purpose, investment beliefs, strategy, and culture enable stewardship that creates long-term value for clients and beneficiaries leading to sustainable benefits for the economy, the environment and society.
	Governance, resources and incentives support stewardship.
	Manage conflicts of interest to put the best interests of clients and beneficiaries first.
	Identify and respond to market-wide and systemic risks to promote a well-functioning financial system.
	Review their policies, assure their processes and assess the effectiveness of their activities.
Investment approach	Take account of client and beneficiary needs and communicate the activities and outcomes of their stewardship and investment to them.
	Systematically integrate stewardship and investment, including material environmental, social and governance issues, and climate change, to fulfil their responsibilities.
	Monitor and hold to account managers and/or service providers.
Engagement	Engage with issuers to maintain or enhance the value of assets.
	Where necessary, participate in collaborative engagement to influence issuers.
	Where necessary, escalate stewardship activities to influence issuers.
Exercising rights and responsibilities	Actively exercise their rights and responsibilities.

FCA – new disclosure requirements on the horizon for managers and contract-based schemes

The FCA is carrying out ongoing climate change and green finance work. Set out below are recent key developments, leading to likely new rules for FCA regulated entities from 2022.

October 2018

A discussion paper on climate change and green finance published setting out a range of proposals, including ensuring those making investment decisions take account of risks including climate change.

October 2019

Response to discussion paper published setting out priorities for future work on climate change and green finance.

December 2019

A policy statement on extending the remit of IGCs published. The statement confirmed the FCA's final rules and guidance, which are set out in the Conduct of Business sourcebook (Independent Governance Committees) Instrument 2019. The rules came into force on 6 April 2020 and introduced new duties for IGCs, including reporting on their firm's policies on ESG issues.

The statement also confirmed related guidance for providers of pension products and investment-based life insurance products on how firms should think about ESG risks, and consumer concerns when making investment decisions on behalf of consumers.

March 2020

A consultation paper published on proposals intended to enhance climate-related disclosures by listed issuers and to clarify existing ESG disclosure obligations. The FCA proposed to introduce a new rule requiring all commercial companies with a premium listing to either make climate-related disclosures consistent with the approach set out by the TCFD or explain why not. The paper closed to comments on 1 October 2020. (Final text now published – see below).

June 2020

The Climate Financial Risk Forum ("CFRF") published a disclosure chapter to the 2020 CFRF Guide.

October 2020

A letter (dated 22 September 2020) was published confirming the intention to consult on implementing disclosures that align with TCFD recommendations for asset managers and contract-based pension schemes in the first half of 2021.

★ It is likely that the rules will be finalised by the end of 2021, with new obligations coming into force in 2022.

October 2020

A speech was delivered by Richard Monks, Director of Strategy, on the ESG reporting regime and how it can be improved. The speech stated that guiding principles are being considered to help firms improve ESG product design and disclosure, based on five proposed supporting principles:

1. Consistency in messaging and approach with regards to a product's ESG focus
2. The clear and fair reflection of an ESG focus in the product's objectives
3. Documented investment strategies to set out clearly how a product's sustainable objectives are to be met
4. Ongoing reporting by firms of their performance against declared sustainable objectives
5. Assurance of ESG data quality by firms

These guiding principles are a key indication of the FCA's preferred approach since it became apparent that the FCA would not be onshoring the Sustainable Finance Disclosure Regulation ("SFDR"). The FCA is expected to consult in 2021 on a UK regime.

December 2020

A policy statement published on its proposals intended to enhance climate-related disclosures by listed issuers and to clarify existing ESG disclosure obligations, along with its final rules and guidance, and the final text of its technical note. The new rules apply in relation to accounting periods beginning on or after 1 January 2021. The technical note applied with immediate effect. The FCA has stated that it plans to issue a follow-up consultation in the first half of 2021 on proposals to extend the rule to a wider scope of listed issuers, and to consider strengthening the compliance basis.

Trustees should watch this space as new obligations will impact the mandated disclosures for their appointed managers. New requirements may also apply to contract-based pension schemes and IGCs.

Sustainable finance disclosures – an EU perspective

Following the adoption of the action plan on sustainable finance in March 2018, the EC has established an EU framework which puts consideration of ESG at the centre of the financial system to help transform Europe's economy into a greener, more resilient system. The EC's package of reforms includes:

The Sustainable Finance Disclosure Regulation[7]	Imposes new transparency and disclosure requirements relating to financial products for financial market participants and financial advisers. The regulations include what firms must disclose and maintain on their websites, what information must be provided to investors, and what should be periodically reported to investors in relation to sustainability factors, policies and risks. This applies at both a manager and product level. Specific disclosure requirements apply to "Article 8 products" (broadly, funds which actively promote environmental or social characteristics) and "Article 9 products" (which have sustainable investment as their objective). Financial market participants with more than 500 employees must also disclose their "principal adverse impacts" using a mandatory and highly prescriptive template. SFDR entered into force on 29 December 2019, however, most of the provisions apply from 10 March 2021.
Taxonomy Regulation[8]	Introduces an EU-wide classification system (or taxonomy) intended to provide businesses and investors with a common language to identify to what degree economic activities can be considered environmentally sustainable. It also imposes new disclosure requirements for certain financial services firms and large public interest entities. The Taxonomy Regulation entered into force on 12 July 2020 with provisions applying from January 2022 and 2023.
Low Carbon Benchmark Regulation[9]	Introduces a regulatory framework that lays down minimum requirements for EU climate transition benchmarks and EU Paris-aligned benchmarks at the EU level. The Low Carbon Benchmark Regulation entered into force on 10 December 2019.

UK application

It appears that the SFDR and the Taxonomy Regulation will not become part of UK law. Although there was initial indication that they would be onshored at the end of the Brexit transition period, a statement made by the Chancellor of the Exchequer (Rishi Sunak), a speech by FCA Director of Strategy (Richard Monks), as well as the omission of the relevant articles from the relevant UK regulations, have suggested otherwise.

However, SFDR remains relevant for UK firms and fund managers. In practical terms, a UK firm may decide to voluntarily comply with the SFDR because of investor pressure. UK firms marketing funds to the EU or managing EU funds may also be within the scope of the SFDR, and UK trustees may wish to seek out funds specifically meeting Article 8 or Article 9 definitions from EU managers. It remains to be seen if the UK will introduce any aspect of the Taxonomy Regulation into UK legislation or, if not, whether there may be some voluntary adoption by UK pension funds and fund managers lacking a UK classification system.

7 Regulation (EU) 2019/2088 on sustainability-related disclosures in the financial services sector
8 Regulation (EU) 2020/852 on the establishment of a framework to facilitate sustainable investment and amending Regulation (EU) 2019/2088
9 Regulation (EU) 2019/2089 amending Regulation (EU) 2016/1011 (BMR) as regards EU climate transition benchmarks, EU Paris-aligned benchmarks and sustainability-related disclosures for benchmarks

How we can help

Sackers is the UK's leading commercial law firm for pension scheme trustees and employers. Over sixty lawyers focus on pensions and its related areas, including Sackers finance and investment group, a team of lawyers who provide cutting edge advice to trustees, employers and providers on all aspects of pension scheme finance and investment.

We advise on the development and implementation of ESG strategies consistent with trustee fiduciary duties and the development of trustee ESG and engagement policies, including how to document trustee responsible investment policies and related disclosures. We also provide ESG training for trustees and pension scheme providers.

For further information and advice on ESG and climate change considerations for UK pension schemes, contact any of the contributors to this guide using the details below, or your usual Sackers contact.

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Abbreviations

AVCs: Additional Voluntary Contributions

CFRF: Climate Financial Risk Forum

DB: Defined benefit

DC: Defined contribution

Disclosure Regulations: The Occupational and Personal Pension Schemes (Disclosure of Information) Regulations 2013

DWP: Department for Work and Pensions

EC: European Commission

ESG: Environmental, social and corporate governance

EU: European Union

FCA: Financial Conduct Authority

FRC: Financial Reporting Council

GHG: Greenhouse gas

IGC: Independent governance committee

ICSWG: The Investment Consultants Sustainability Working Group

IIGCC: Institutional Investors Group on Climate Change

Investment Regulations: The Occupational Pension Schemes (Investment) Regulations 2005 (as amended)

IORP II: Directive (EU) 2016/2341

IPCC: UN Intergovernmental Panel on Climate Change

LDI: Liability-driven investment

PCRIG: Pensions Climate Risk Industry Group

PLSA: Pensions and Lifetime Savings Association

PRI: Principles of Responsible Investment

SFDR: Sustainable Finance Disclosure Regulation (Regulation (EU) 2019/2088)

SIP: Statement of investment principles

SRD II: Directive (EU) 2017/828 (which amended the Shareholder Rights Directive)

TCFD: Task Force on Climate-related Financial Disclosures

TKU: Trustee knowledge and understanding

TPR: The Pensions Regulator

UKSIF: United Kingdom Sustainable Investment and Finance Association

WACI: Weighted Average Carbon Intensity

Further reading

DWP response to consultation (June 2021): Taking action on climate risk: improving governance and reporting by occupational pension schemes

PCRIG guidance (January 2021): Aligning your pension scheme with the TCFD recommendations: a guide for trustees

TPR: Consultation document on: Guidance on governance and reporting of climate-related risks and opportunities, and A new appendix to TPR's monetary penalties policy (July 2021)

TCFD Final Report (June 2017): Recommendations of the TCFD See also the TCFD Knowledge Hub

PRI Implementing the TCFD Recommendations: A Guide for Asset Owners (2018) See also the Principles for Responsible Investment: PRI | Home

IIGCC: Navigating climate scenario analysis – a guide for institutional investors – IIGCC (February 2019)

Accounting for Sustainability case studies (including BBC Pension Trust: approach to scenario analysis (January 2021); and HSBC Pension Scheme putting in place TCFD metrics (January 2021): Knowledge hub

PLSA: Implementation Statement guidance for trustees (July 2020)

ICSWG: Guide for assessing climate competency of Investment Consultants (January 2021)

The Transition Pathway Initiative: Home – Transition Pathway Initiative

IPCC: Intergovernmental Panel on Climate Change

Science Based Targets initiative: Ambitious corporate climate action – Science Based Targets

ShareAction: Point of No Returns series – A ranking of 75 of the world's asset managers approaches to responsible investment

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