Getting to net zero

A spotlight on the role of pension trustees

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Introduction

Stuart O'Brien
Partner
stuart.obrien@sackers.com

Welcome to our latest guide for pension trustees on climate change, a subject of profound importance to society and an ever increasing focus for asset owners.

In 2016, we launched our first practical guide for trustees on how ESG could be incorporated into pension scheme investment strategies. Since then, the industry and the regulatory environment has moved on apace and each year we have tried to bring clarity to this topic with an updated guide covering the latest requirements and legal thinking. Last year, we focused on the disclosure aspects of ESG and climate change, reflecting the raft of new climate reporting obligations being introduced under the Pension Schemes Act 2021. You can find all our previous guides on our website plus more information for trustees still grappling with the Occupational Pension Schemes (Climate Change Governance and Reporting) Regulations 2021.

This year, we wanted to do something a bit different and so, getting away from the regulations for a moment, we are focusing on net zero.

Net zero has become something of a standard for trustees looking to nail their ESG colours to the mast, but it's not always clear what is meant by such a commitment, nor what trustees should be thinking about when deciding whether to make one. It looks good on paper, but what is really involved in the implementation of a net zero commitment? The legal considerations can also be something of a grey area.

That is why we are really excited to be bringing out this latest spotlight, designed specifically for trustees who are considering making a net zero commitment. We cover some of the legal aspects to think about, including the old chestnut of trustee fiduciary duties. We also wanted to provide a practical slant to things and that is why we are pleased to have contributions from a number of industry experts.

On pages 14-16, Edwin Whitehead from Redington gives the investment consultant perspective on how trustees can implement a net zero investment strategy in practice. And, on pages 20-23, we're delighted to share some real world insight from Brian Kilpatrick from HSBC and Padmesh Shulka from TfL from the trustee perspective.

Finally, on pages 24-25, Luba Nikulina from Willis Towers Watson and Amanda Latham from Barnett Waddingham provide an overview of some of the cross-industry work being carried out by the Net Zero Investment Consultants Initiative (NZICI). In particular, they look at how trustees should be broaching the subject with their investment consultants.

We hope you enjoy reading this guide and that it helps you on your journey to net zero.

Download our previous ESG guides from our website.

What is net zero?

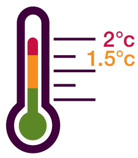
Put simply, "net zero" refers to achieving a balance between the amount of greenhouse gas (GHG) emissions produced and the amount of GHG removed from the atmosphere. When human activities add no more GHG emissions than we take away, we reach net zero.

Achieving net zero is important as, to eventually stop global warning, net additions of GHG into the atmosphere have to reach zero.

Where did the concept of net zero come from?

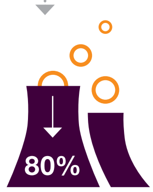
With net zero now being a mainstream concept, it is easy to forget how far it has come in a short period of time.

A decade ago, the concept of net zero was still confined to the scientific community. The term only started to become more widely used following the adoption of the Paris Agreement in December 2015.



The Paris Agreement established goals of keeping global average temperature rises to well below 2°C above pre-industrial levels and aiming for 1.5°C. In order to meet these goals, signatories undertook to make rapid reductions in GHG emissions to aim to achieve net zero GHG emissions in the second half of the century.

In 2018, the IPCC Special Report on the Impacts of Global Warming at 1.5°C concluded that in order to keep global warming to a temperature rise of 1.5°C, GHG emissions need to be at net zero around 2050, or around 2070 for a 2°C rise.



Since then, the concept has taken off and, in June 2019, the Government amended the Climate Change Act 2008 to commit the UK to achieving net zero by 2050 (in contrast to its previous target of an 80% reduction in GHG emissions by 2050).

What would a net zero target look like for a pension scheme?

For an asset owner, setting a net zero target means identifying a point in time by which the net GHG emissions of all companies invested in will be zero. In order to be meaningful, a long-term net zero target will usually have interim targets for emissions reductions from a baseline level.

Importantly, adopting a net zero target would not necessarily mean that trustees could only invest in businesses which have achieved GHG neutrality themselves. The key is that the net emissions of the portfolio are balanced so, in the future, GHG intensive businesses may still be held as long as those emissions can be offset elsewhere by carbon capture or other emerging technologies.

What is the law on net zero?

Under the Pension Schemes Act 2021 and the accompanying Occupational Pension Schemes (Climate Change Governance and Reporting) Regulations 2021 (the Climate Change Governance Regulations), trustees of in-scope schemes are required to meet certain governance and disclosure obligations in respect of climate-related risks and opportunities which underpin the TCFD recommendations (see page 11 for further detail).

However, to date, the Government has steered away from imposing mandatory net zero targets on pension schemes[1] and the Climate Change Governance Regulations do not require trustees to set them (or any other mandatory targets to reduce portfolio emissions).

That said, a number of bigger schemes have chosen to adopt a net zero target for their investments over the past year (an approach which has been commended by TPR in its Climate Change Strategy) and this is increasingly an area which trustees are keen to explore.

The member perspective

As more schemes are starting to explore how they can align to net zero, an increasing number of members are taking an interest in how their own pension savings are invested. Organisations like Make My Money Matter (MMMM) have been successfully campaigning to get members more engaged with their pensions savings and to ask questions about responsible investment.

Trustees are not obliged to act on member views – indeed the law is actually quite restrictive on the extent to which they can properly be acted on in investment decisions at all.[2] However, that does not mean that trustees should not engage with their membership and those trustees who have properly considered climate change and taken steps that are appropriate for their pension schemes will be best placed to do so and to respond to member scrutiny.

When engaging with members and responding to questions, trustees should consider the following:

- what information trustees have a legal obligation to provide.[3] This should be provided at a minimum but there may be merit in going further. Trustees may have a good story to tell and can use their responsible investment approach or net zero commitment to positively engage with their scheme's membership
- of course, some members may remain unsatisfied with the answers they have received or the investment approach being taken. In that case, a formal complaint will always be a possibility. In that case, wider disclosures may well be required – ie by formal disclosure in proceedings in litigation. TPR also has wide-ranging investigative powers that can require the disclosure of documentation. So, when considering a member's initial request, it is worth bearing in mind the possible consequences of not providing some information voluntarily (although trustees should always consider whether there are any confidentiality or legal privilege concerns or restrictions)
- always respond promptly and with genuine engagement. Even where it is not legally necessary to provide information requested or directly respond to any questions posed, genuine engagement (even if limited and brief) is likely to result in a better outcome for everyone concerned.

1 See page 7 for details of the proposed amendment to the Pension Schemes Bill in June 2020, which was voted down by Government benches

2 See our 2019 ESG Guide on putting the law into practice for more detail

3 See our 2021 ESG Guide to trustee disclosures for more detail

The net zero story

September 2013 – the IPCC Fifth Assessment Report concludes that in order to eventually stop global warming, net additions of GHG into the atmosphere would need to reach zero.

December 2015 – the Paris Agreement established goals of keeping global average temperature rises to well below 2°C (aiming for 1.5°C) and to achieve net zero GHG emissions in the second half of the century.

June 2017 – TCFD publishes its Final Report setting out its recommendations in relation to climate-related disclosures.

October 2018 – the IPCC Special Report on the Impacts of Global Warming at 1.5°C concludes that in order to limit temperature rises to 1.5°C, GHG emissions need to be at net zero around 2050.

May 2019 – the Paris Aligned Investment Initiative (PAII) is established by the IIGCC.

June 2019 – the Climate Change Act 2008 (2050 Target Amendment) Order 2019 is passed which increased the UK's commitment to a 100% reduction in emissions by 2050.

July 2019 – Government publishes its Green Finance Strategy setting out its proposals on the role of the financial sector in delivering global and domestic climate objectives.

February 2020 – Government-backed amendments to the (then) Pension Schemes Bill laid before parliament that included new regulation-making powers regarding climate – related governance and disclosures.

June 2020 – further amendments to the Pension Schemes Bill proposed by opposition peers and MPs which would have required trustees specifically to take account of the Paris Agreement in their investment strategies. In November, this proposal was debated in the Commons where 256 MPs backed the change, but this was not sufficient to carry the amendment with the majority on the Government benches voting against.

July 2020 – Nest, the UK's largest pension scheme by membership, sets out its plans to be net zero across its investments by 2050 or earlier.

September 2020 – the world's largest GHG emitter, China, commits to achieving net zero carbon emissions before 2060.

October 2020 – the BT Pension Scheme commits to net zero emissions by 2035.

November 2020 – ShareAction propose a draft Responsible Investment Bill which includes mandatory net zero for DC default funds marketed as sustainable as well as imposing new duties on TPR and the FCA consistent with net zero.

February 2021 – the Pension Schemes Act 2021 receives royal assent, paving the way for increased climate change governance and reporting obligations on trustees.

March 2021 – IIGCC launches The Net Zero Investment Framework, providing a common set of recommended actions, metrics and methodologies through which investors can maximise their contribution to achieving global net zero emissions by 2050 or sooner.

April 2021 – TPR sets out its Climate Change Strategy.

1 June 2021 – MMMM launches the world's first Net Zero Pension Summit.

30 September 2021 – House of Commons Work and Pensions Committee publishes Fourth Report of Session 2021–22 on Pension stewardship and COP26, recommending that TPR establish a working group to develop guidance for schemes looking to set net zero targets.

October 2021 – the Climate Change Governance Regulations come into force, requiring trustees to meet the climate change governance requirements which underpin the TCFD recommendations and publish an annual report on how they have done so.

October 2021 – DWP issues a consultation seeking views on proposals to require trustees of authorised schemes to measure and report on the "Paris alignment" of their portfolios.

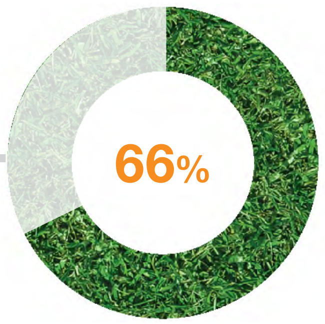
18 October 2021 – HMT publishes its policy paper "Greening Finance: A Roadmap to Sustainable Investing".

19 October 2021 – BEIS publishes the Government's long-awaited Net Zero Strategy.

31 October to 13 November 2021 – COP26 takes place, concluding in the signing of the Glasgow Climate Pact (which sets out a series of resolutions which build on the Paris Agreement and sets out what needs to be done to tackle climate change) and the agreement of the Paris rulebook (which gives guidance on how the Paris Agreement is delivered).

2 November 2021 – HMT publishes Fact Sheet: Net Zero-aligned Financial Centre, providing guidance on climate (or net zero) transition plans.

December 2021 – the Government confirmed in response to the House of Commons Work and Pensions Committee Fourth Report of Session (see above) that it will not be establishing a working group to develop guidance for schemes looking to set net zero targets, nor would it consult on the case for mandating alignment with UK Government climate goals.



April 2022 – over two thirds of countries (66%) have made net zero pledges.[4]

4 Net Zero Tracker | Welcome

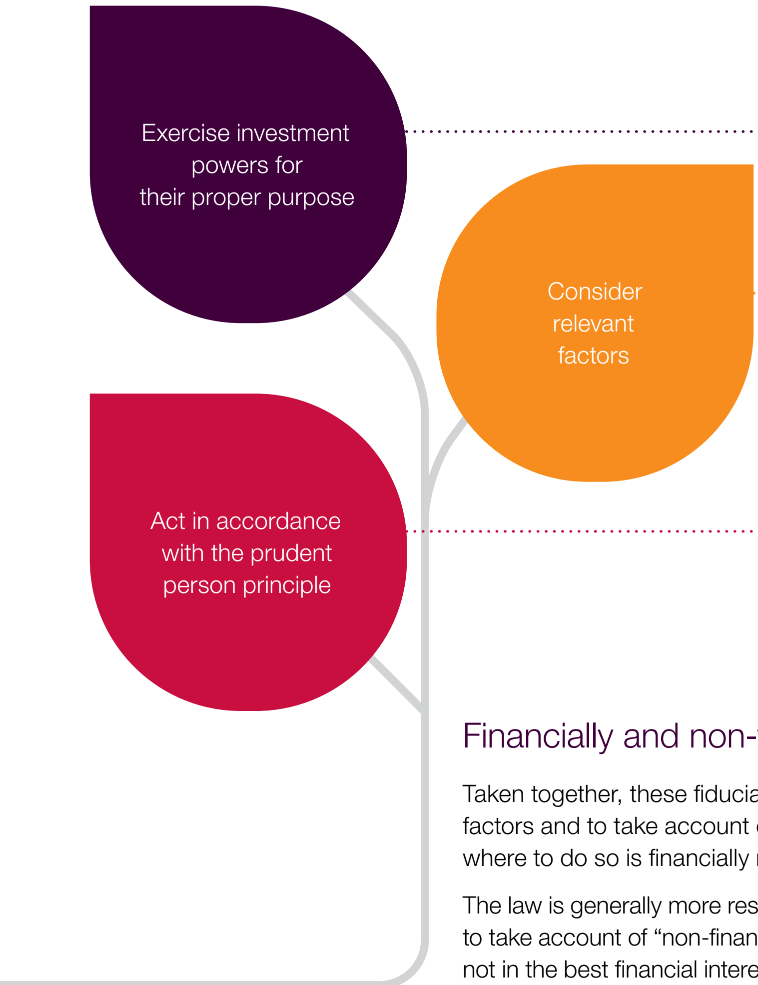
How does net zero align with fiduciary duty?

Fiduciary duty of pension trustees

In previous guides, we have looked at trustees' fiduciary duties and their compatibility with ESG issues.

In our view, there is no doubt that trustees can take account of ESG issues as financial factors in their investment decision making. Indeed, we would advise that trustees are under a positive obligation to take account of such factors where material and as part of their trusts law and fiduciary duties.

Broadly speaking these legal duties require trustees to:



Exercise their investment powers for their "proper purposes", namely the provision of members' pensions.

Take account of factors which are relevant to that purpose, which will usually mean those which are financially material (this may be consideration of risks as well as returns).

Do so in accordance with the "prudent person" test – broadly this is the principle that trustee investment powers must be exercised with the "care, skill and diligence" a prudent person would exercise, when dealing with investments for someone else for whom they feel "morally bound to provide."

Financially and non-financially material factors

Taken together, these fiduciary duties will usually act as good reason for trustees to act on ESG factors and to take account of climate-related risks and opportunities in their investment strategy, where to do so is financially material.

The law is generally more restrictive on the circumstances in which it is permissible for trustees to take account of "non-financial" factors in making any investment decisions where these are not in the best financial interests of the scheme's beneficiaries. Non-financial factors may include expressions of moral disapproval, political or ethical motivations or furthering of external purposes not directly attached to the pension scheme and the financial best interests of its beneficiaries.

The distinction between financial factors which trustees are legally able to take into account and "non-financial" factors, which they generally cannot (at least not without surmounting particularly high legal hurdles), is not always a bright line. Many issues, including those relating to climate change, will have both financial and non-financial aspects. Further, some issues that start out as non-financial may become financial. The key is that trustees must base their investment decisions on what is financially relevant to the pension scheme in relation to the applicable time horizon being considered, which in the context of pension schemes may be many years.

Trustees' consideration of any net zero commitment must be taken in this context – ie such a commitment should be made where trustees consider that the commitment (and the actions that follow from making it) will support financially the provision of members' pensions from their pension scheme.

Understanding climate change as a financial risk

In the absence of policies to reduce emissions of GHGs (such as net zero commitments), global warming is expected to reach 4.1°C – 4.8°C above pre-industrial levels by the end of the century (the "baseline scenario"). Current policies presently in place around the world are projected to reduce baseline emissions and result in about 2.7°C warming.[5] Temperature rises at any of these scales, however, would have large and detrimental impacts on global economies, society and investment portfolios.

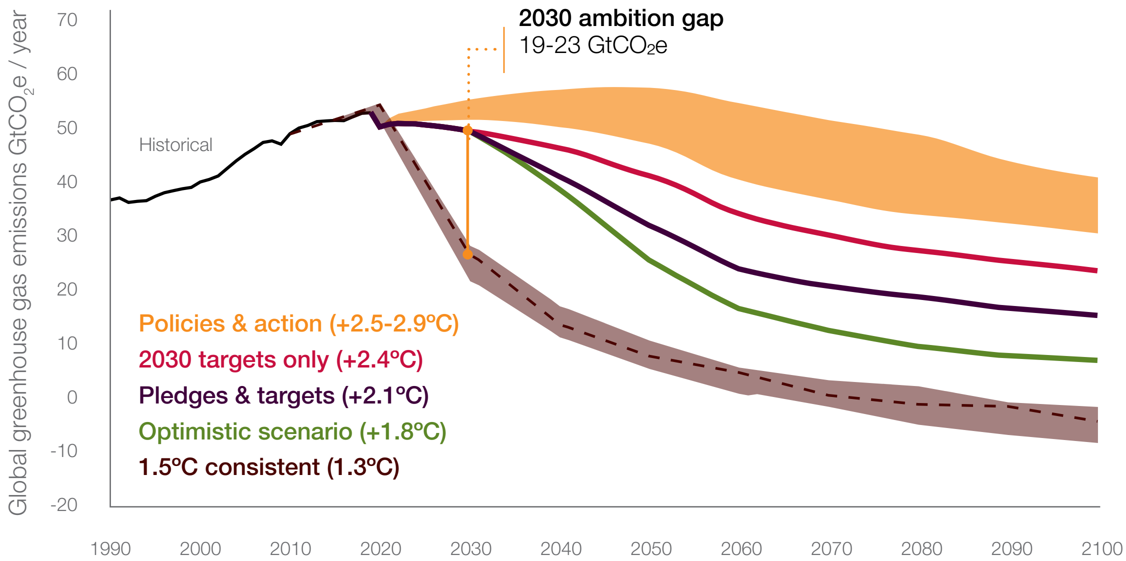
Keeping temperature rises to well below 2°C above pre-industrial levels in line with the Paris Agreement (and the pursuit of efforts to limit these even further to 1.5°C) requires a rapid reduction in GHG emissions in the coming years, and to net zero around the middle of the century. This will require a significant change in the fundamental structure of the global economy.

As investors, all pension schemes are exposed to financial risk from these issues. Higher global temperatures and more extreme weather events pose physical risks to assets, but perhaps of even greater significance to investors is the market impact of the required transition to a net zero economy.

As can be seen from the chart below, if we are to keep temperature rises to those aspired to in Paris, a fundamental shift in how all businesses and society operate will be required. For an investor, some businesses invested in may be well positioned for this transition and some will not.

2100 Warming Projections

Emissions and expected warming based on pledges and current policies



Source: Climate Action Tracker, November 2021

5 Temperatures | Climate Action Tracker

Considering a net zero commitment as a financial factor

A net zero commitment may be capable of being considered within the parameters of financial factors as set out above.

Ultimately, it will be up to the trustees and their investment advisers to consider whether a net zero commitment (and the actions that follow from making it) will support financially the provision of members' pensions. However, the following points may assist in making such an assessment.

- There is a reasonable expectation that governments and policy makers will seek to deliver on their commitments to achieve net zero and that doing so will require a significant change in the fundamental structure of the economy at national and international levels. Trustees may reasonably take into account the financial risks to their pension scheme of holding an investment strategy that is not aligned with this anticipated global transition.
- Trustees are not bound to "call" the global economic transition precisely before making their own investment decisions. Adopting the principles outlined above as part of the "prudent person" test, trustees may reasonably consider the merits of an aligned investment strategy in contrast to a non-aligned one. On this, consideration may be given to the risk of an Inevitable Policy Response, as described by the PRI.[6]
- Trustees may also reasonably consider the climate-related opportunities of a global economic transition to a low carbon economy and the extent to which investment advice would support the investment opportunities consistent with a net zero commitment.

Trustees may also be tempted to ask whether they can take wider factors into account, such as the impact their actions may have on their members' quality of life or the wider economy. However, this is a particularly difficult legal area. We provide some commentary on this on page 18, but trustees would always need to consider this carefully with their own legal advisers.

Conclusions

A net zero commitment may be adopted by trustees where it is considered to be consistent with the primary purpose of the pension scheme of paying members' pensions.

Trustees can act prudently in making their investment decisions and may reasonably base their assessment of what a prudent investment strategy for their pension scheme would be on an expectation that governments and policy makers will seek to deliver on their commitments to achieve net zero. Although trustees should take investment and legal advice on this, this may support a net zero commitment as part of a prudent investment approach.

The making of a net zero commitment should not fetter the future investment discretion of trustees and should be considered as an overall objective. Trustees should retain an ability to determine, in respect of any given investment decision, what is in the best financial interests of their pension scheme.

6 A climate transition forecasting consortium commissioned by the PRI which "aims to prepare institutional investors for the portfolio risks and opportunities associated with an acceleration of policy responses to climate change" forecasts that an acceleration in climate policy will be increasingly forceful, abrupt, and disorderly

How does net zero fit with the new climate change regulations, metrics and targets?

New climate reporting obligations were introduced in 2021 under the Pension Schemes Act 2021 (the Climate Change Governance Regulations).

The new requirements are being phased in, with larger schemes whose net assets are £5bn or more, and master trusts, already required to comply. Schemes with £1bn or more of assets will be required to comply from 1 October 2022.

Trustees of schemes in scope are required to put in place appropriate governance arrangements to manage climate-related risks during the first scheme year in which the Climate Change Governance Regulations first apply to them. They must then produce and publish an annual report on how they have done so (the Report) within seven months of their scheme year end date (for further information see our Guides and Alert).

The Climate Change Governance Regulations focus on improving climate change risk, governance and reporting, in line with TCFD recommendations. They include requirements on selecting and reporting on climate-related metrics and setting targets in respect of at least one of these metrics. In practice, meaningful disclosures on climate will not be possible without trustees undertaking certain governance activities, and for the first time the Climate Change Governance Regulations not only tell affected trustees what they must disclose on ESG matters, but also prescribe specific actions that must be taken first. As noted on page 7, a mandatory net zero requirement had been proposed during the legislation's passage into law, but ultimately did not make it into final legislation. However, as noted on page 12, amendments to the legislation already look set to introduce some reporting of scheme alignment, albeit without mandatory targets.

Requirements under the Climate Change Governance Regulations (reminder)

Under the regulations, trustees must:

Governance

- establish and maintain, on an ongoing basis, oversight of the climate-related risks and opportunities which are relevant to the scheme
- establish and maintain processes for the purpose of satisfying themselves that persons undertaking governance activities on their behalf (and/or who advise or assist the trustees in respect of governance), are taking adequate steps to identify, assess and manage any climate-related risks and opportunities which are relevant to the scheme.

Strategy

- identify and assess, on an ongoing basis, the impact of climate-related risks and opportunities which they consider will have an effect over the short, medium and long term on the scheme's investment strategy.

Scenario analysis

- as far as they are able, undertake scenario analysis assessing the impact on the scheme's assets and liabilities and the resilience of the scheme's investment strategy, for at least two climate scenarios.

Risk management

- 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.

Metrics and targets

- select certain climate-related metrics to monitor and report on an annual basis. The current requirement is that such metrics should include at least one absolute emissions metric and one emissions intensity metric, as well as one additional climate change metric. However, amendments to the Climate Change Governance Regulations proposed by the DWP would require trustees to additionally obtain and report on a fourth "portfolio alignment metric" describing the extent to which their investments are aligned with the goal of limiting the increase in the global average temperature to 1.5°C above pre-industrial levels (see below)
- set a non-binding target for the scheme in relation to at least one of their chosen metrics, and, so far as they are able, measure and report performance against it on an annual basis. It should be noted, however, that the requirement to set a target does not necessarily mean that trustees must set a target to reduce their emissions. Other targets, such as improving data quality, are equally permissible under the regulations. The statutory guidance also makes clear that long-term targets (eg net zero by 2050) will not be sufficient to meet the regulatory target-setting requirements without shorter-term interim targets.

New alignment metric for pension scheme investors

On 21 October 2021, the DWP published a consultation paper that puts forward proposals which will require trustees of schemes in scope of the new governance and reporting obligations to measure (as far as they are able) and report on their investment portfolios' alignment with the Paris Agreement. The paper also consults on draft statutory and non-statutory guidance that seeks to clarify stewardship and ESG issues for trustees.

The DWP has noted that many UK occupational pension schemes have voluntarily adopted a net zero target. However, it considers that a further alignment metric is nevertheless necessary, "highlighting firms which are furthest from alignment with climate goals or which make the biggest contributions to climate change".

Ahead of the consultation, on 14 October 2021, the TCFD also published updated implementing guidance and new guidance on metrics, targets and transition plans that support companies in making disclosures and linking them to financial impacts. The updated guidance includes a recommendation that financial institutions disclose the extent to which their assets are aligned with a well-below 2°C scenario, in line with the goals of the Paris Agreement.

The DWP broadly proposes to adopt the TCFD's updated guidance by amending the Climate Change Governance Regulations to require trustees in scope to calculate and disclose a metric describing the extent to which their investments are aligned with the Paris Agreement goal of limiting the increase in the global average temperature to 1.5°C above pre-industrial levels. This new portfolio alignment metric will therefore be a fourth metric in addition to the three existing metrics already mandated.

As drafted, all trustees who are subject to the Climate Change Governance Regulations would have to comply with the new requirements from 1 October 2022. This would include schemes that are part-way through a scheme year.

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Today we’re leading the world yet again in becoming the first major economy to pass new laws to reduce emissions to net zero by 2050 while remaining committed to growing the economy – putting clean growth at the heart of our modern Industrial Strategy.

Chris Skidmore June 2019

The Climate Change Governance Regulations prescribe matters that trustees must consider and disclose but do not oblige any particular investment approach.

In particular, although there is a regulatory requirement to monitor a number of prescribed climate-related metrics and to set a target in relation to one of these, this need not necessarily include an emissions-based reduction target. There is no regulatory obligation to set a net zero target.

Consequently, the regulations should be considered neither a reason for, nor against, trustees adopting a net zero commitment.

Broader Government initiatives on “greening finance”

In June 2019, the Government said it was the first major economy in the world to pass laws to bring all greenhouse gas emissions to net zero by 2050. There have been several moves to achieve this goal, setting the backdrop for regulations specific to occupational pension schemes.

On 18 October 2021, HMT published its policy paper “Greening Finance: A Roadmap to Sustainable Investing”. The paper set out the Government’s ambition to green the financial system and align it with the UK’s net zero commitment. The paper builds on the Government’s 2019 Green Finance Strategy and indicates that asset managers, regulated asset owners and listed companies will be required to publish transition plans that consider the Government’s net zero commitment, or provide an explanation if they have not done so.

Following this, on 2 November 2021, HMT published Fact Sheet: Net Zero-aligned Financial Centre, providing guidance on climate (or net zero) transition plans. This guidance provides more detail on what a transition plan is and what will be required. The Government considers that a transition plan should include the high-level targets that the organisation is using to mitigate climate risk, including GHG reduction targets (ie a net zero commitment).

As standards for transition plans start to emerge, the Government has confirmed it will take steps to incorporate these into the UK’s Sustainability Disclosure Requirements and strengthen requirements to encourage consistency in published plans and increased adoption by 2023. The guidance does however clarify that it is not requiring firms to adopt mandatory net zero targets.

Paris Aligned Investment Initiative (PAII)

The PAII was established in May 2019 by the IIGCC. By March 2021, the initiative had become a global collaboration supported by four regional investor networks (AIGCC (Asia), Ceres (North America), IIGCC (Europe) and IGCC (Australasia)). The PAII now involves over 110 investors representing over $34 trillion assets.

The initiative commits assets owners to decarbonising their pension funds and investment portfolios, and to scaling up investment in climate positive initiatives. The commitment must be aligned with the goals of the Paris Agreement of a 1.5°C decarbonisation target, alongside the setting of interim targets for both emissions reductions and investments.

Trustees may wish to support any net zero commitment by becoming a signatory to the Paris Aligned Investment Initiative Net Zero Asset Owner Commitment (the PAII Net Zero Commitment). It should be noted, however, that the PAII Net Zero Commitment contains a number of specific commitments in relation to how signatories are expected to implement net zero and trustees will need to ensure that they are comfortable with all of these before signing up.

Redington: making real progress on a net zero journey

Edwin Whitehead, CFA
Senior Vice President,
Sustainable Investment

Edwin.Whitehead@
redington.co.uk

REDINGTON

The landscape has changed for UK pension trustees considering the risks associated with climate change. Although global efforts to mitigate the impact of a changing climate are progressing, it is at a much slower rate than what is required according to scientific consensus. Stark geopolitical risks and a post-pandemic recovery means we may have to face the fact that the transition to net zero will not be an orderly one.

These are "big picture" issues. On a smaller scale, trustees are coming to terms with the challenges associated with following the latest climate regulations. Data quality considerations, scenario analysis and carbon metrics are new to many trustees. However, through this noise, more and more schemes are asking their advisers to help them take positive action in building an integrated approach to their net zero journey. We suggest a two step approach.

Step one: measurement

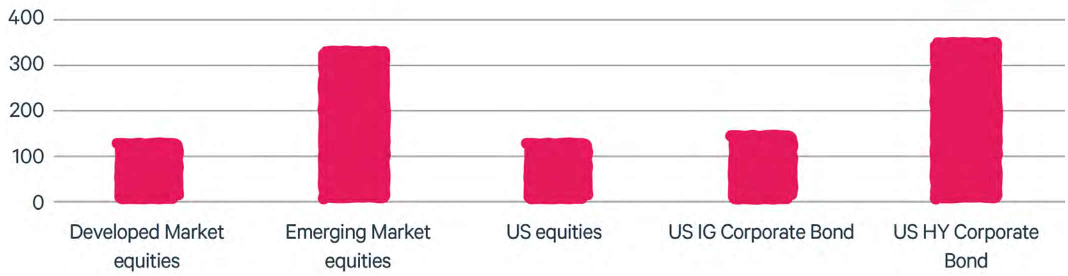
Net zero is a destination. The journey, therefore, has a starting point. Measuring this starting point is a real challenge. Data quality is poor and incomplete, methodologies differ and there is no formal accounting standard for GHG emissions. These challenges are not exclusive to UK trustees, they are felt on a global scale. While it is therefore important to recognise these issues, it is equally important to acknowledge that they will be solved over time. A good place to start is to understand where the biggest emitters are. We have found estimating asset class emissions informative, as not all asset classes have similar emissions profiles.

In equities, emerging markets will naturally be more emissions-intensive due to their heavily industrial economic base. Credit can also be very emissions-intensive, especially in high yield. This is because companies with asset-heavy balance sheets tend to finance with debt, and so high yield indices tend to have a higher relative weight to the industrial and energy sectors. These industries tend to generate far greater emissions than technology companies, for example, which dominate developed market equity indices.

Recognising these broader relationships rather than getting bogged down in the challenges of data and measurement allows time to focus on quick wins and the strategic asset allocation decisions that contribute towards achieving a net zero portfolio.

Weighted Average Carbon Intensity

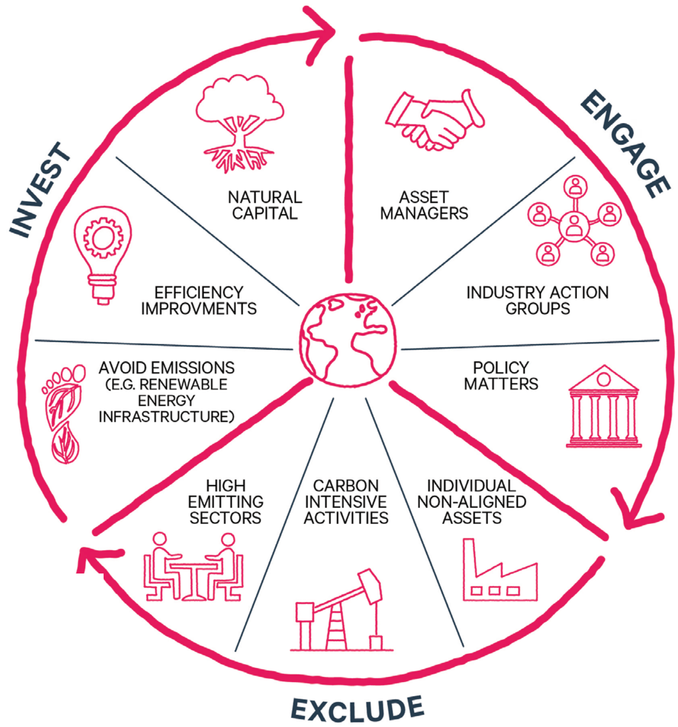
(Scope 1+2) (tCO_2e/$m sales)

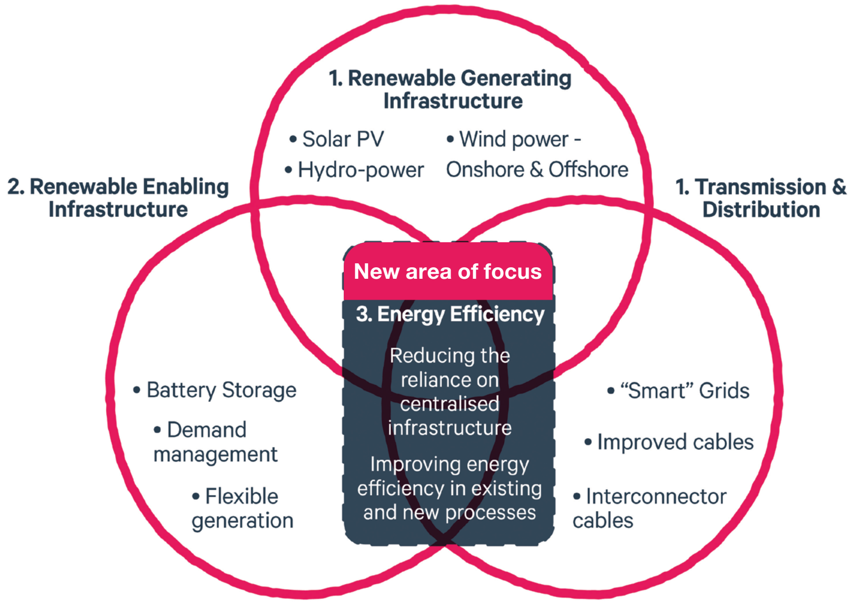


Source: MSCI. As at 30 September 2021

Step two: taking action

Achieving a net zero objective requires investing with a different mindset. Simplistically, there are three levers trustees can use to achieve their goals. The first of these is investing (putting money to work), the second is effectively engaging with invested assets, and the third is removing investment from assets that are not aligned with achieving said goals.





Invest – now is the time

As a global community, we need to change the way we produce and consume energy. Financing this transition has, and will, create an abundance of investment opportunities. We have already seen a shift in where the most attractive investment opportunities lie: Redington clients have allocated in excess of £2bn to renewable energy infrastructure. Demand for these assets has risen considerably, having a positive impact on returns but, in turn, making prices seem less attractive now.

Key themes are emerging as part of this transition, such as the decentralisation of power production and improved energy efficiencies. Renewable energy producing infrastructure is being brought closer to the end consumer, and efforts to maximise energy usage are being scaled up. One driver of this is corporations setting their own decarbonisation objectives and building up their resilience against volatile power price markets. For example, large technology companies need to build fully green data centres consistent with their net zero objectives. These smaller-scale projects can mitigate material development risks and offer attractive, contractual returns. In addition, more traditional renewable infrastructure projects continue to require funding, as do emerging technologies. The industry is rapidly evolving, and investors need to be nimble and open to new ideas.

Engage – but mind the gap

To achieve global climate goals, long-term sustainable investors must engage with invested companies to align their business models with the required transition to net zero. However, for many pension trustees, good stewardship can seem like a free lunch – engagement responsibilities can be delegated to their asset managers. However, given the state of the climate emergency, it is evident this delegation of responsibilities has failed us to date. So, how can we do better? A simple approach would be better measurement and accountability – but be sure to mind the gaps.

Engaging for reductions in real-economy emissions is challenging and not likely to be achieved instantaneously. However, using standardised, independent metrics overseen with academic rigour means the current position of companies can be assessed, and improvements tracked.

Redington recommend that their clients use at least one of the following metrics:

	Climate Action 100+	Transition Pathway Initiative	Science Based Targets
Coverage	167 companies covering 80% of corporate industrial emissions	479 companies but increasing	Over 2,000 companies taking action
Advantages and limitations	+ Can be used to assess state of alignment fully	+ Can be used to assess state of alignment mostly	+ Methodology is based on science-based climate pathways
	+ Based on public disclosures	+ Based on public disclosures	– Can be used to assess state of alignment partially
	+ Good coverage in terms of global emissions	– Limited coverage in terms of companies	– Voluntary initiative, it requires companies to work with the SBTi
	– Limited coverage in terms of companies	– Accessibility of data	– Accessibility of data
	– Accessibility of data		

These metrics can be used to measure the progression of some of the world's largest emitters. Of course, coverage is limited, but as we said with data issues more broadly, this problem exists for everyone, we should not let it stop us from taking action now. Asset managers must judge whether a company has a credible transition plan and monitor whether they are delivering on it – that is the core measure of whether net zero will be delivered by engagement.

These measures can also be used to direct asset manager engagements. In our experience, asset managers are not always engaging with the most material emitters or the largest companies in a portfolio, so challenging them to report against these metrics should encourage more targeted engagements, covering more of a portfolio's footprint.

There is also a gap in engaging with debt issuers alongside equity issuers. We have shown that a lot of the emissions problem exists in the debt markets – however, with no associated ownership rights, managers may renege on their engagement responsibilities.

Reviewing these two engagement gaps (coverage of material emitters and debt versus equity) can unearth which parts of a portfolio resources should be focused on, and which managers could do better.

Exclusion – the final straw

If all escalation steps have been taken and the desired outcome is not achieved, the decision to exclude or divest from the company should be considered. This should be treated as a means of risk management, where an investment has become misaligned with your investment goals.

We believe this lever should be reserved for those investments that are most misaligned – often carbon-intensive fossil fuel activities such as thermal coal and unconventional oil and gas. While the need to transition is strong, given recent events, so is the short-term supply and longer-term resilience of energy. This is why divestment must come at the end of a long process of engaging with the company; it should indicate the investor's loss of trust in the capabilities of management to execute a low-carbon business strategy.

Bring the levers together

A divestment decision would free up capital that can be reallocated, or invested into new opportunities, thus completing the circle of this simple framework: invest impactfully in financially attractive opportunities, engage with what you own and sell when your engagements are not effective.

We have fewer than three decades to achieve a monumental transition in the way we produce and consume things. We are already going in the wrong direction. Now is the time to act.

Net zero – the bigger picture

"A rising tide lifts all the boats"

The above phrase is commonly attributed to John F. Kennedy, who first used it in a speech in 1963, although it appears that he may have borrowed it from the New England Council's regional chamber of commerce. The central premise, however, is that an improved economy will benefit all participants and that government economic policy should therefore focus on broad economic efforts.

Whether this way of thinking can be applied to trustee investment decision making is increasingly being asked in the context of pension schemes considering their commitment to net zero.

On pages 8-10, we explored the compatibility of trustee fiduciary duties with net zero commitments, noting that trustees must exercise their investment powers for the purposes of paying members' pensions and taking account of relevant (usually financially material) factors. But can trustees apply these principles to prevent the companies they invest in from engaging in business strategies that have a negative impact on people and planet, thereby improving the chances of their members retiring into a <2°C world?

Considering external impact

With ESG considerations now mainstream, the investment community has generally bought into the idea that companies which do harm to the environment may suffer from increased regulatory risk to their own business models, while companies with sustainable business practices better aligned to a net zero carbon future may present an improved financial proposition for a long-term investor. However, considering the wider external impact that companies have on communities and the environment for its own sake has generally been a separate consideration reserved for a particular type of impact investor.

On a conventional view of fiduciary duties and ESG, trustees can clearly look at the financial prospects for the company in question, but what if a company's bad behaviour actually boosts its financial performance? What should trustees do then? Should the fact that a company "externalises its costs" in a way that will damage the environment or reduce society's chances of a net zero economy be a relevant factor that trustees can or should take account of, even where this can't be shown to have a detrimental effect on the company itself?

The market paradox

Whilst there are clear advantages to a relatively free market economy, we know things can go badly wrong if companies can derive profit, not just from improving efficiency and innovation, but from activities that transfer costs to other companies, social institutions, or the environment.

Most large asset owners, such as pension funds, generally have diversified investment portfolios and rely on healthy social and environmental systems to support their broad portfolios. For such an investor this externalisation of costs by offending investee companies might risk dragging down the overall performance of a wider investment portfolio as well as damaging the world into which the scheme's members expect to retire. Reducing our chances of hitting net zero in time might also heighten physical risk from extreme weather events to other assets owned by the investor (eg properties).

For some very large investors, who consider themselves to be "universal owners" of diversified portfolios representing a slice of the overall market, these wider portfolio impacts are already starting to be recognised in their investment decision making, which seeks to foster the good health of the overall economy upon which their investment returns depend.

The Universal Owner

> **The Universal Owner hypothesis is based on the idea that there are clear links between the performance of large, diversified investment portfolios and the economy overall. It states, "a portfolio investor benefiting from a company externalising costs might experience a reduction in overall returns due to these externalities adversely affecting other investments in the portfolio, and hence overall market return". For a diversified investor, there is no place to hide from these costs: they come back into the portfolio as taxes, insurance premiums, inflated input prices and the physical cost of disasters.**
>
> SEITCHIK, A. (2007) CLIMATE CHANGE FROM THE INVESTOR'S PERSPECTIVE

Taking account of wider factors

On pages 8-10, we identify that trustees should take account of relevant factors in their decision making. In our view, there are sound legal arguments why taking account of wider considerations – damage to the wider economy and even members' quality of life – could be "relevant" factors to be taken into account by pension trustees consistent with the purpose of the pension scheme.

The difficulty, however, is that while such aims may be relevant to a scheme and its beneficiaries (and potentially also the scheme's other investments), it can be difficult to demonstrate that an investment decision taken in order to protect the wider economy will in practice further that objective other than for very large institutional investors.

This point was considered (albeit briefly) by the Law Commission in its 2014 report.[7]

> **6.53 — In some circumstances, damage to the wider economy might be considered a financial factor, as it will impact on the scheme's portfolio as a whole… In the [Consultation Paper] we said that the aim of a pension fund is to secure returns across the whole portfolio. Therefore there can be no legal objection to making a decision which, after due consideration, is designed to provide financial benefits to the portfolio as a whole… However, for the decision to be justified on financial grounds, the anticipated benefits to the portfolio should outweigh the likely costs to the portfolio. In other words, the financial benefit must not be "too remote and insubstantial" and must accrue to the fund itself, not to the social good in a more general way.**

The key wording here, which in our view correctly states the legal position, is that the benefit **must accrue to the pension scheme itself**. Taken as an individual investment decision (by one set of pension trustees to make a relatively small investment allocation decision away from a particular industry or sector or towards a climate-related opportunity in furtherance of a net zero objective) it may be hard to demonstrate the causal link between that decision and the wider economic benefits delivered. However, there is at least some scope, in our view, to take account of the trustees' decision as part of a wider collective action of institutional investors to invest for net zero.

In practice, this is somewhat akin to recognising the game theory conundrum of the "prisoner's dilemma".[8]

7 Law Commission report: Fiduciary Duties of Investment Intermediaries (30 June 2014)

8 The "prisoner's dilemma" game was described by Albert W. Tucker (see "The Mathematics of Tucker: A Sampler." The Two-Year College Mathematics Journal, vol. 14, no. 3, 1983, pp. 228–32)

The prisoners' dilemma

The classic prisoner's dilemma goes like this:

Two members of a gang of bank robbers have been arrested and are being interrogated in separate rooms. The authorities have no other witnesses and can only prove the case against them if they can convince at least one of the robbers to betray his accomplice and testify to the crime. Each bank robber is faced with the choice to cooperate with his accomplice and remain silent or to defect from the gang and testify for the prosecution.

- If they both co-operate and remain silent, then the authorities will only be able to convict them on a lesser charge resulting in one year in jail for each (= 2 years total jail time).
- If one testifies and the other does not, then the one who testifies will go free and the other will get five years (0 years for the one who defects + 5 for the one convicted = 5 years total).
- However, if both testify against the other, each will get two years in jail for being partly responsible for the robbery (= 4 years total jail time).

	Prisoner A testifies	Prisoner A stays silent
Prisoner B testifies	Both get 2 years in prison	Prisoner A gets 5 years, prisoner B goes free
Prisoner B stays silent	Prisoner A goes free, prisoner B gets 5 years	Both get 1 year each

In this case, each robber always has an incentive to defect, regardless of the choice the other makes. From A's point of view, if B remains silent, then A can either co-operate with B and do a year in jail, or defect and go free. Obviously, he would be better off betraying B and the rest of the gang in this case. On the other hand, if B defects and testifies against A, then A's choice becomes either to remain silent and do five years or to talk and do two years in jail. Again, obviously, he would prefer to do the two years over five.

The paradox of the prisoner's dilemma is this: both robbers can minimize the jail time only if they both co-operate and stay silent (2 years total), but the incentives that they each face separately will always drive them each to defect and end up doing the maximum jail time of 4 years total.

Looking at pension trustees as potential drivers of financial markets towards net zero, the incentives faced by each individual trustee board (and based on the conventional legal analysis of fiduciary duty above) might induce them to invest only so far as it can be established that an investee company can "do well by doing good." But this alone may not be nearly enough to address the systemic risks we face while investors continue to resist asking individual companies to sacrifice at least some financial return for the good of the economy overall.

Acting cooperatively, however, could make investors collectively better off by engaging robustly with companies that might otherwise drag the side down and supporting financially those that might offer the wider economy the best chance of success in a net zero world.

These are undeniably big and difficult questions that push against the boundaries of any conventional interpretation of trustee fiduciary duties but nobody said net zero was going to be easy. And as schemes start thinking about how they turn net zero commitment into action it is these sorts of "bigger picture" questions that trustees and the pensions advisory community will need to tackle.

Net zero in practice: a conversation with our clients

Q&A with HSBC: making a net zero commitment

Brian Kilpatrick
Chief Investment Officer, Pension Scheme Executive,
HSBC Bank Pension Trust (UK) Limited

brian.kilpatrick@hsbc.com

What motivated the trustee board to make a net zero commitment?

The trustee has an established policy that managing the risks associated with climate change is part of its fiduciary duty to factor all material financial risks into its investment strategy. The trustee has also long been a public supporter of the Paris Agreement as a means to mitigate the dangerous effects of climate change and has published an annual TCFD report since 2018. Setting a net zero commitment was a natural progression in the trustee evolving their approach to climate risk management.

How did the board approach things from a governance perspective?

In 2020 we documented an ESG risk management policy, which, amongst other things, established the necessary roles and responsibilities across our decision making bodies. However, we recognised that more resource was required given the complex nature of net zero commitments. We therefore established a Climate Risk Working Group ("CRWG") comprised of our advisers, the trustee board and the pension scheme executive to identify strategic targets relating to climate-related risks and opportunities pertinent to the scheme. This group met monthly, with a specific terms of reference: to recommend to the board a robust and appropriate net zero commitment.

As the CRWG was preparing its recommendation, we made sure the whole trustee board was fully trained and informed on issues specific to net zero, including new metrics and the underlying science behind the environmental challenges. This meant the trustee board was ready to make an informed decision when the CRWG made its recommendation in September 2021.

Why did the Trustee decide to use the PAII framework?

We have a policy of supporting sustainable investment organisations that are aligned with our goals. As such, we have been members of the IIGCC for over five years and joined the PAII in October 2021 when we made our net zero commitment. We strongly advocate frameworks and metrics that are appropriate for asset owners managing diverse, multi-asset portfolios. The Net Zero Investment Framework designed by the PAII provides the direction and structure to implement a net-zero investment strategy.

Also, as supporters of the Paris Agreement which was signed at the 21st COP in 2015, we were watching closely the outcomes of last year's COP26 in Glasgow, as these were vital to the overall Paris goals still being attainable. We therefore wanted to align our commitment, as part of the Glasgow Financial Alliance for Net Zero (GFANZ), with this global coalition of leading financial institutions' commitment to accelerating the decarbonisation of the global economy. By making a commitment as part of Glasgow Financial Alliance for Net Zero – which includes the PAII, it meant to us that our commitment is credible and consistent, but we also make ourselves accountable for taking action. We are in the process of creating our first Climate Action Plan which we will publish a year following our commitment. This will then be reported against in our annual TCFD report in subsequent years.

How did the approach differ for the scheme's DB and DC sections?	▶	We made sure the approach was consistent for both DB and DC and so our commitment is based on the type of assets; listed credit and equity, rather than by scheme type. We anticipate the implementation of the commitment to differ between DB and DC. This is due to the greater control over the investment strategy and mandate design the trustee has for the DB assets. The DC assets are expected to grow in size materially over the next decade, whereas the closed DB benefits will fall in size. Therefore it was important for the trustee to understand that the absolute emissions of the DC assets may grow, and so the carbon efficiency – or absolute emissions per unit of investment is the metric that must fall. This nuance did not apply to the shrinking DB benefits.
Were there any trustee/sponsor dynamics to manage?	▶	The trustee has a good relationship with the sponsor and socialised the CRWG work stream outputs and its conclusions, as well as the press release content prior to making its net zero announcement. The trustee and the sponsor are keen to stay aligned as far as possible on their respective net zero journeys recognising the differences in the investment assets they have stewardship over, differences in direct control over those assets and the range of stakeholders to which they are respectively accountable.
How is progress going to be measured and reported?	▶	The state of alignment of the underlying investments with achieving the goals of the Paris Agreement is a central measure for us to monitor to determine whether we are on track to achieve our goals and where engagement needs to be targeted. However, gathering the right data, and applying the right metrics is a real challenge. We are keeping an open mind and pushing our asset managers to report against metrics that are independent and overseen with academic rigour. We bring these metrics together, alongside broader carbon metrics and approximations of our exposure to transition and physical risks in a scheme-wide dashboard. The dashboard is still in its infancy, but aims to show how the trustee is performing versus its climate objectives. The progress of this journey will be reported against annually in our TCFD statement.
How are you engaging the scheme's members?	▶	The trustee has published ESG educational materials in its website to inform members on how it is attempting to manage and mitigate climate risk in its investment strategy and will ask the members a series of ESG related questions in the 2022 member questionnaire. This will be followed by future updates on the scheme website and in the annual member newsletter.

What tips would you have for other schemes looking at making similar commitments?

- ✓ When starting the process, recognise the inherent uncertainty with the subject.
- ✓ Be aware that data quality is poor, and there is limited consensus on the best quality metrics.
- ✓ Recognise that decision makers are having to deal with these imperfections and it can be a challenge to accommodate this degree of uncertainty in the strategic planning of decarbonisation pathways.
- ✓ We suggest trying to meet these challenges with high quality, and consistent training. There are lots of good resources available, and the transition to more digital ways of working means, in our experience, trustees are comfortable with pre-recorded videos, and shorter more targeted sessions.

Q&A with TfL: making a net zero commitment

Padmesh Shulka, CFA
Chief Investment Officer Pensions, TfL Pension Fund

PadmeshShukla@tflpensionfund.co.uk

What motivated the trustee board to make a net zero commitment?

The trustee board was motivated by the fund's green investment beliefs that explicitly recognise climate change as a long-term risk and see no conflict between sustainability and return maximisation. The board was equally mindful of the fund's high profile public nature and strong expectations from its key stakeholders, particularly members, to act responsibly and with due prudence, considering the long duration of the fund's liabilities.

How did the board approach things from a governance perspective?

The board realised quite early on, as far back as 2016, that it was important to have a clear framework, approach and strategy towards climate change and sustainability more broadly and that was only possible if the board owned this issue from a governance perspective. As a first step, climate related beliefs, as outlined above, were added to the existing beliefs after extensive debates and discussions. This provided the foundation for more work to be undertaken inhouse (this was critical, as this activity was deemed too important to be outsourced to our advisers; instead it was a partnership involving the advisers and some of the largest investment managers with interest in this area) to plot the challenges and opportunities, providing greater clarity and confidence over time to finally commit to ambitious net zero targets.

Were there any trustee/sponsor dynamics to manage?

This was a complex, but an extremely engaging, process. The fund office ran a series of workshops with the trustees where these targets were debated and discussed, with the investment consultants providing helpful external perspective and challenge. The trustees were provided a range of options with their pros and cons, covering everything from deliverability to issues around trust and ambition, and informed decisions were made based on science based targets and the fast evolving regulatory framework.

Transport for London, the sponsor, was hugely supportive of the fund's net zero targets as it sat well with its own ambitions, reputation awareness and broader stakeholder expectations from London's quite progressive, demanding and climate aware population base. The sponsor was entirely cognisant and respectful of the independence of the trustee decision making process, so did not directly take part in the target setting but provided whole-hearted support to the Net Zero Framework, once it was agreed.

How is progress going to be measured and reported?

The targets are long-term but they would be tracked internally by the fund office using actual emission measures (scope 1 and 2) for public securities and proxies/estimates for asset classes where the data is unavailable. In this regard, the fund is leveraging technology to its benefit whereby the entire fund sits on industry leading Aladdin platform with climate feeds coming from multiple data providers.

In addition, the fund would also undertake scenario testing by using publicly available tools like TPI and BOE Stress Tests. It would also use its partnership with its managers to undertake sustainability mapping of the fund's portfolio to UN's Sustainable Development Goals Framework, amongst other things.

Finally, voting and engagement is going to be a very important area for the trustees to work with the companies to nudge long-term responsible actions and adoption of green business models. Most of these measurements and actions are shared with the trustees at least on a quarterly basis and would be reported on an annual basis.

How are you engaging the scheme's members?

Communication was identified as an area for improvement around five years ago. It had become quite clear that a "trust us" approach would not work, with members not entirely happy with our disclosures and transparency around our strategy and actions in this area. The SIP was seen as a compliance document, helpful but not very insightful, leaving scope for better explanation.

The trustee board opened up our work to our stakeholders with the publication of the fund's first sustainability report in 2018, which is now published every December and is freely available on our website. It has completely changed our relationship with our stakeholders. They can now see what we are doing, recognise the areas we are looking to do more, and appreciate the challenges involved. The report has been welcomed and embraced by everyone, helping to build trust with our key stakeholders. This was extremely important as we knew the net zero journey would not be linear and would have to be adapted as we go along.

What tips would you have for other schemes looking at making similar commitments?

- ✓ It is important to start somewhere, acknowledging there will be gaps in knowledge, science and understanding.
- ✓ Everyone's journey will be unique to their circumstances and that is also fine because there are no absolute "rights" or "wrongs".
- ✓ Keep an open mind and be ready to adapt as more information and clarity emerges around so many know unknowns.
- ✓ Think about net zero both from an opportunity and risk basis.

NZICI: working with your consultant

Luba Nikulina
luba.nikulina@
willistowerswatson.com

Amanda Latham
amanda.latham@
barnett-waddingham.co.uk

ICSWG INVESTMENT CONSULTANTS SUSTAINABILITY WORKING GROUP

The role of investment consultants in net zero implementation

Investment consultants are responsible for advising their clients on the investment of trillions of dollars of capital across the world. How this capital is invested will be key to whether or not we are able to achieve the global goal of net zero emissions by 2050 or sooner.

Investment consultants usually work with institutional asset owners, such as pension funds, sovereign wealth funds, insurance companies, endowments, foundations and family offices. They provide strategic advice to help clients achieve their investment objectives, subject to the client's investment beliefs, responsible investment policies and risk parameters. Consultants will advise clients on asset allocation (eg equities vs bonds vs alternatives) as well as implementation (eg active management vs index tracking).

Investment consultants do not research individual securities but instead help their clients select the most suitable asset management firms to implement their strategies. As such, investment consultants are the critical link between asset owners and asset managers, providing education and analysis to asset owners, together with guidance to asset managers about product design based on the consultant's knowledge of asset owners' needs.

In real world terms, investment consultants bring together multiple asset owners and multiple asset managers to encourage innovation and help create new investment solutions. Investment consultants provide advice either on a non-discretionary basis, where asset owners take all decisions, or on a discretionary basis, where asset owners delegate most or part of their decision-making power to an investment consultant. Some investment consultants provide only non-discretionary advice, others only discretionary services, and some provide a combination of both.

When thinking about net zero investing, trustees should be looking for relatively advanced skills and knowledge from their investment consultant to help achieve effective net zero alignment and avoid unintended issues. For example, a focus solely on carbon emissions can drive particular behaviours – investors may be tempted to sell their highest emitting assets to reduce their portfolio emissions, however this action may have no impact at all on global emission levels if the assets are acquired by other investors. Instead, forward-looking metrics should be used to help identify investments that may not be low carbon today, but where companies are taking action to decarbonise and have credible commitments, targets and plans in place. Metrics and methodologies are still developing and expected to standardise over time, with some areas better developed than others.

In selecting their investment consultant, pension fund trustees and other decision makers need to ensure that their consultants have built and are able to maintain effective levels of climate competence to support the advice they give and the implementation of that advice, as this is an area that continues to evolve rapidly. The Investment Consultants Sustainability Working Group (ICSWG), a group of leading UK investment consulting firms with the aim of seeking to improve sustainable investment practices across the investment industry, has developed a guide for assessing climate competency of investment consultants to help clients identify consultants who are more likely to be able to effectively support the implementation of their clients' net zero ambitions. Trustees should use this guide to ask their advisers for evidence of the actions they have taken to support the reported competencies when they are selecting or reviewing their investment consulting services and target those who are closer to the best practice indicators.

Investment consultants can help clients across many areas of net zero implementation by:

- ✓ working with clients to help them develop their understanding of the real world and financial implications of climate change and to articulate their investment beliefs on climate change
- ✓ developing climate scenarios showing the impacts of physical and transition risks on clients' investments
- ✓ facilitating clients' understanding of risks and opportunities associated with climate change and decarbonisation of the global economy
- ✓ helping clients reflect net zero alignment in their asset allocation and portfolio construction decisions
- ✓ helping clients select asset managers and design products that provide better alignment with net zero
- ✓ helping with stewardship and engagement, developing policies, undertaking engagement with asset managers and monitoring their activities on behalf of investors
- ✓ providing monitoring services showing the current state and progress towards net zero alignment
- ✓ engaging with regulators, standard setters and cross-industry initiatives on behalf of clients and supporting clients in their own regulatory and cross-industry engagement and collaboration.

2021 saw the launch of a multitude of worldwide net zero initiatives. The global Race To Zero campaign is looking to mobilise actors outside of national governments to join the Climate Ambition Alliance to accelerate the necessary transformation to reach the goals of the Paris Agreement and stabilise the global temperature rise to 1.5°C. The campaign focuses on representing cities, regions, businesses, investors, and higher education institutions.

In the lead up to the COP26 climate conference in 2021, GFANZ, backed by Race to Zero, developed a global coalition of leading financial institutions committed to accelerating the decarbonization of the economy and reporting annually on activities and outcomes achieved. The net zero initiatives include the Net Zero Investment Consultants Initiative (NZICI). These initiatives are designed to push the boundaries as well as to provide a forum for collaboration to move the things forward faster, so you are going to be more likely to get the most recent thinking along with fit for purpose capabilities from investment consultants that are part of the NZICI.

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.

Stuart O'Brien
Partner
D +44 20 7615 9539
E stuart.obrien@
sackers.com

Key areas of expertise include: ESG issues including fiduciary duties, policy, stewardship, responsible and impact investing. Also advises on risk transfer strategies including buy-ins and buy-outs. Chair of PCRIG.

Ralph McClelland
Partner
D +44 20 7615 9532
E ralph.mcclelland@
sackers.com

Key areas of expertise include: risk transfer transactions including buy-ins and buy-outs, fiduciary management, custody arrangements, all types of pooled investment products and ESG, including stewardship and climate change issues.

Jacqui Reid
Partner
D +44 20 7615 9550
E jacqui.reid@
sackers.com

Key areas of expertise include: DC investment strategy, regulation and industry best practice for IGCs and providers, member engagement and value for money.

Paul Phillips
Partner
D +44 20 7615 9523
E paul.phillips@
sackers.com

Key areas of expertise include: risk transfer, LDI, longevity transactions, investment management agreements, transition and custody arrangements.

Emma Martin
Associate Director
D +44 20 7615 9574
E emma.martin@
sackers.com

Key areas of expertise include: DC policy and regulation for occupational schemes, master trusts, IGCs and providers.

Andrew Harper
Associate
D +44 20 7615 9575
E andrew.harper@
sackers.com

Key areas of expertise include: risk transfer transactions including buy-ins and buy-outs, pooled investment funds, ESG issues and reporting, DC regulation. Member of PCRIG.

Hannah Savill
Associate
D +44 20 7615 9534
E hannah.savill@
sackers.com

Key areas of expertise include: risk transfer transactions including buy-ins and buy-outs, ESG issues and reporting and data protection issues.

Leanne Carter
Associate
D +44 20 7615 9519
E leanne.carter@
sackers.com

Key areas of expertise include: advising on amendments to the governing documentation of schemes, interpreting pensions legislation and guidance, ESG and governance issues.

Abbreviations

AIGCC: Asia Investor Group on Climate Change

BEIS: Department for Business, Energy and Industrial Strategy

BOE: Bank of England

Climate Change Governance Regulations: The Occupational Pension Schemes (Climate Change Governance and Reporting) Regulations 2021

COP26: The 26th UN Climate Change Conference of the Parties

DB: Defined benefit

DC: Defined contribution

DCIF: Defined Contribution Investment Forum

DWP: Department for Work and Pensions

ESG: Environmental, social and corporate governance

FCA: Financial Conduct Authority

GFANZ: The Glasgow Financial Alliance for Net Zero

GHG: Greenhouse gas

HMT: HM Treasury

IGC: Independent governance committee

ICSWG: Investment Consultants Sustainability Working Group

IGCC: Investor Group on Climate Change (Australasia)

IIGCC: Institutional Investors Group on Climate Change

IPCC: UN Intergovernmental Panel on Climate Change

LDI: Liability driven investment

MMMM: Make My Money Matter

NZICI: Net Zero Investment Consultants Initiative

PAII: Paris Aligned Investment Initiative

PCRIG: Pension Climate Risk Industry Group

PLSA: Pensions and Lifetime Savings Association

PPI: Pensions Policy Institute

PRI: Principles for Responsible Investment

SBTi: Science Based Targets initiative

SIP: Statement of investment principles

SPP: The Society of Pension Professionals

TCFD: Taskforce on Climate-related Financial Disclosures

TPI: Transition Pathway Initiative

TPR: The Pensions Regulator

Further reading

Accounting for Sustainability: ESG Maturity Map: Example Behaviours for Pension Trustees, Aligning to a net zero pathway – top tips for pension scheme trustees

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

IIGCC: Net zero investment framework 1.5˚C Implementation Guide (March 2021)

Institute and Faculty of Actuaries: Sustainability

IPCC: Special Report on the Impacts of Global Warming at 1.5°C (October 2018); Climate Change 2014: Synthesis Report (2014); Sixth Assessment Report (April 2022)

Net Zero Tracker (updated periodically)

LGIM: Net Zero – A practical guide for investors (2021)

MMMM: Green Pensions Charter

PCRIG Climate Guide: Aligning your pension scheme with the Taskforce on Climate-Related Financial Disclosures recommendations (January 2021)

PLSA: ESG and Stewardship: A Practical Guide to Trustee Duties (June 2019)

PPI: ESG: past, present and future (October 2018)

PRI: UN-convened Net-Zero Asset Owner Alliance; Principles for Responsible Investment: PRI | Home

ShareAction: Assessing Net Zero and Paris Alignment Claims (July 2021)

SPP: ESG Guide (2021)

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

TPR: Climate change strategy (April 2021)

UK Parliament: House of Lords Library: Climate change targets: the road to net zero? (May 2021)

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Sackers

Sacker & Partners LLP
20 Gresham Street
London EC2V 7JE
T +44 20 7329 6699
E enquiries@sackers.com
www.sackers.com