



HM Government

Aligning your Pension Scheme with the TCFD Recommendations

Part II - Quick Start Guide

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The Pensions Climate Risk Industry Group



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Quick Start Guide: Trustee governance, strategy and risk management: how to integrate and disclose climate-related risks

TCFD can be applied to consideration and action on climate risk at every stage of the investment journey.

1. Setting investment beliefs

When developing their investment beliefs, the trustee board should clarify their position on climate change considerations and the appropriate types of actions they might take by asset class. Under TCFD, they should formalise and document their governance policies, including roles, in relation to climate change.

2. Considering climate risks in setting investment strategies, reviewing and reporting

Trustees should consider how different investments and strategies could be impacted by transition and physical risks, at an asset class, sector and firm level where appropriate.

Schemes should set out what risks and opportunities they consider to be relevant or material to them over the short/medium/long term time horizons for their scheme. They should use scenario analysis (see module 3 and associated quick start guide) as a helpful tool.

In developing mandates and selecting pooled funds, trustees should identify strategic actions to reduce exposure to climate-related risks, as well as options for investment in climate-related opportunities.

Growth assets are more sensitive to climate-related risks than income-generating assets, but this will vary by sector and firm preparedness –some sectors (for example renewables and electric vehicles) and assets (such as green infrastructure) will benefit from the low-carbon transition.

Asset managers' climate competence should be factored into manager selection, and be monitored post-appointment. Trustees should also ensure that investment consultants demonstrate a robust track record in assessing and addressing climate risk, and have adapted their core services to include consideration and discussion of long-term risks and opportunities.

Asset managers and consultants should demonstrate consideration of climate risk management through both investment strategy and engagement. Signatory status and reporting against the Principles for Responsible Investment (PRI) and 2020 UK Stewardship Code are key minimum expectations for both managers and consultants.

Trustees should factor climate change into their monitoring and review of asset managers, by assessing performance against any climate-related objectives, benchmarks and targets, as well as the quality of voting and engagement, disclosures and scenario analysis. Trustees can use the 'Top 10' suggested questions in the Annex to rigorously assess the capabilities and approach to climate management of new and existing managers in line with TCFD recommendations.

Under TCFD, trustees should document how they identify and assess the materiality of climate-related risks and opportunities, document the main risks and opportunities for each time horizon and their potential impact, and explain their assessment of their scheme's resilience to different scenarios, including relevant metrics and targets. They should also identify, document and disclose how climate issues are included in their consultants' objectives, and in the selection, review and monitoring of asset managers.

3. Stewardship

Trustees should be clear on how stewardship fits within the scheme's investment strategy and how it helps them meet their climate-related objectives. Where they delegate to asset managers, trustees should carry out due diligence, ensure their approaches are in line with the trustees', set expectations, and hold managers to account. Where schemes carry out their own engagement, trustees should articulate clear policies and processes, making systematic use of all voting powers, and where they will support or requisition climate-related resolutions. Trustees with fewer resources for specific activities can increase their influence by joining in collaborative engagement efforts.

Trustees should document and disclose their own stewardship policies, report on how they have followed them, and hold investee companies to account on doing TCFD.

4. Additional points to consider for DB schemes

Climate change can have significant implications for the strength of the sponsor's covenant. Where sponsors are part of, or dependent on, the high-carbon economy, trustees should be aware that their scheme will likely have above-average exposure

to climate-related risks. Weather-related events will affect others, for example, through impacts on supply chains or production facilities.

DB liabilities may be affected by impacts on inflation rates and demographic factors, particularly longevity. Trustees should take a holistic approach and look at how climate risks around the employer covenant, funding and investment strategy are all linked and inter-dependent, through integrated risk management (IRM).

Trustees should ask the sponsoring employer for its TCFD disclosures or equivalent information, include climate considerations in its regular covenant monitoring between valuations, and have contingency plans so they can take decisive action if and when required.

Under TCFD, trustees should identify and assess the materiality of climate-related risks and opportunities to their sponsoring employer, the main risks and opportunities for each time horizon and their assessment of their employer's resilience to different scenarios.

5. Method of reporting and member communications

Trustees not in scope of UK regulations can include their TCFD review in the annual report and accounts, or a chair's statement, implementation statement, or a standalone report. Those in scope must publish their TCFD report on a freely accessible public website and provide a link to it in the annual report and accounts.

Trustees can also consider including more tailored member communication on climate change in regular newsletters or social media output. There is growing evidence to show that communicating clearly with members on how climate-related risks and opportunities are being managed can also help build trust and public confidence.

Top 10 questions for Asset Managers

1. Has the manager produced a TCFD report which outlines their governance of climate related issues? (Governance)
2. Will the manager share climate-related scenario analysis undertaken as part of their investment process? (Strategy)
3. Do they support shareholder resolutions on climate change - if so, how many, which ones, and what was the rationale for their decision? (Strategy)
4. Are they transparent regarding all their voting activity? (Strategy)
5. What is the manager's escalation policy when engagement is unsuccessful? Can they give an example of when they have escalated, how they did so, their rationale for doing so, and the outcome? (Strategy)
6. Does the manager support and/or play a leading role progressive public policy initiatives on climate change, e.g. decarbonisation of transport, agriculture? (Strategy)

7. How does the manager undertake top-down research and analysis related to climate-related risks? (Risk Management)
8. Does the manager demonstrate that the implications of climate-related risks are considered across different asset classes and investment strategies? (Risk Management)
9. Do they know, and disclose, the exposure to fossil fuel assets? (Risk Management)
10. Does the manager commit to providing trustees with appropriate (and fund specific) climate metric data required to permit the trustees to meet their own disclosure obligations? (Metrics and Targets)