

The Department for Work and Pensions

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Dear Sir / Madam,

## **The Department for Work and Pensions' ("DWP"): Taking action on climate risk: improving governance and reporting by occupational pension schemes – response and consultation on regulations (the "Consultation"; the "Regulations")**

Lincoln Pensions Limited ("Lincoln Pensions" or "we"), the leading specialist provider of employer covenant advice to sponsors and trustees of UK defined benefit ("DB") pension schemes, is pleased to respond to the Consultation which was issued by the DWP in January 2021.

### **About Lincoln Pensions**

Our clients are responsible for around £300bn of scheme assets in aggregate, including some of the largest DB pension funds in the UK and many with material exposure to climate change risks. We advise clients on all aspects of employer covenant and are part of the Cardano Group, the purpose-built investment and risk specialist, operating in the UK and the Netherlands. This submission is made by Lincoln Pensions. Cardano Risk Management Limited has provided a separate response.

We confirm that you may publicly acknowledge our response to the Consultation.

### **Our response to the Consultation**

We have not responded specifically to the questions raised in the Consultation (in keeping with our October 2020 response) as they largely relate to pension investments and so are not directly relevant to our experience.

However, having provided direct feedback to you through e-mail correspondence in October / November 2020 on the importance of assessing climate risk in respect of the covenant, we welcome the confirmation in the Consultation / Regulations that ***"For many schemes, the strength of the covenant is key to their funding strategy and, therefore, it is important that trustees understand the potential impact of climate change and related policy change... on the covenant"***.

We agree that, given the complexities, uncertainties and range of potential outcomes of climate change, ***“Trustees should use scenario analysis to better understand the potential impact on the covenant of the effects of climate change”.***

We also agree with your assertion that obtaining information as part of a scenario analysis process, even confidential information, should be no different or more onerous than in the course of a normal covenant assessment; we would highlight that there is much information in the public domain that trustees can use to build an understanding of the exposure of the covenant to climate risk, particularly with respect to qualitative risk assessment.

We believe that the Consultation / Regulations could possibly go further regarding the application of proportionate scenario testing to the employer covenant of smaller schemes than those that are currently ‘in-scope’. Whilst we appreciate that the costs for smaller schemes associated with complying with the Regulations may not be demonstrably outweighed by the benefits at this stage, particularly in the initial phase of the Regulations, we believe that the risk of climate change on the employer covenant is something that all schemes should consider at some level.

To not do so could expose the members of smaller schemes to what is likely to be a seismic shift in covenant strength for many schemes without having appropriately prepared, and we note that other regulations and requirements apply to all defined benefit schemes irrespective of size. We believe that there are cost-effective ways for schemes of all sizes to build an understanding of the exposure of their covenant to climate change and would be pleased to discuss this topic with you.

**We therefore believe that the DWP and the Pensions Regulator (“TPR”) should jointly consider either:**

- 1. Extending the range of which DB pension schemes are ‘in scope’; or**
- 2. Incorporating the covenant aims of the Consultation as a feature of TPR’s guidance (through the upcoming revisions to the DB funding code, TPR’s Annual Funding Statement or TPR’s impending climate strategy in relation to the recent Pension Schemes Act).**

The latter option, of incorporating the aims of the Consultation in TPR guidance, could encourage trustees of schemes that are not ‘in scope’ to consider climate risk to the employer covenant without having to incur the full costs of complying with the Regulations (e.g. reporting, etc.).

We hope our comments are helpful and we would be pleased to discuss our response with the DWP.

Yours faithfully,



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