DWP Consultation – Taking action on climate risk: improving governance and reporting by occupational pension schemes

Response on behalf of the Friends Provident Pension Scheme

6 October 2020

This response has been approved by the chair of the scheme's trustee board. The scheme currently has more than £1.5bn in assets, and is therefore directly affected by the proposals. The scheme fully supports the management and reporting of climate related risks in its assets, and prior to recent DWP announcements and this consultation, was planning to publish its first TCFD report in 2021. Having learnt from other asset owners that have already published TCFD reports, we intended to start our reporting with governance and strategy, to be followed by risk management and metrics and targets in future years. The proposals in this consultation would require us to accelerate that plan, which we are happy to do.

Having noted our support for the management and reporting of climate related risks, we are wary of this becoming a process where compliance takes precedence over quality, to the detriment of achieving changes in asset owner and corporate behaviours.

Question 1
We propose that the following schemes should be in scope of the mandatory climate governance and Task Force on Climate-related Financial Disclosures (TCFD) reporting requirements set out in this consultation:

a) trust schemes with £1 billion or more in net assets
b) authorised master trusts
c) authorised schemes offering collective money purchase benefits

Do you agree with our policy proposals?

We agree that these schemes should be in scope. We also expect to see other pension schemes and asset owners included, for example LGPS and other funded public sector schemes, and insurers.

Question 2
We propose that:

a) trustees of schemes with £5 billion or more in net assets on their first scheme year end date to fall on or after 1 June 2020 are subject to the climate governance requirements from 1 October 2021 and the trustees must publish a TCFD report within 7 months of the current scheme year end date or by 31 December 2022 if earlier
b) trustees of schemes with £1 billion or more in net assets on the first scheme year end date to fall on or after 1 June 2021 are subject to the climate governance requirements from 1 October 2022, and the trustees must publish a TCFD report within 7 months of the current scheme year end date, or by 31 December 2023 if earlier
c) trustees of master trust or collective money purchase schemes which are authorised on 1 October 2021 are subject to the climate governance requirements with immediate effect, and the trustees must publish a TCFD report in line within 7 months of the current scheme year end date, or by 31 December 2022

After 1 October 2021:

d) trustees of master trust or collective money purchase schemes which become authorised are subject to the climate governance requirements with immediate effect, and the trustees must publish a TCFD report within 7 months of the current scheme year end date
e) where schemes cease to require authorisation, the climate governance and TCFD-aligned reporting requirements fall away with immediate effect, unless they remain in scope via the asset threshold on the previous scheme year end date

From 1 June 2022 onward:

f) trustees of schemes not already in scope of the requirements and with £1 billion or more in net assets on any subsequent scheme year end date:

are subject to the climate governance requirements starting from one year after the scheme year end date on which the £1 billion asset threshold was met
must publish a TCFD report within 7 months of the end of the scheme year from which the climate governance requirements apply
g) trustees of schemes in scope of the requirements whose net assets fall below £500m on any subsequent scheme year end date cease to be subject to the climate governance requirements with immediate effect (unless they are an authorised scheme) but must still publish their TCFD report for the scheme year which has just ended within 7 months of the scheme year end date

Do you agree with the policy proposals?

Broadly yes, except that the requirement to publish the report "within 7 months of the current scheme year end date, or by 31 December 20xx if earlier" is more challenging for any scheme with a year end after 31 May each year, and increasingly problematic the later the year end date in the calendar year.

For example, our scheme year ends on 30 September, which means that we will have only three months each year to produce our TCFD report. This is likely to be very problematic in the first year of production, and to some extent every year, given inevitable time lags in acquiring data for the metrics and targets section of the report.

Question 3
Subject to Government deciding to adopt any of the governance or reporting requirements proposed in this consultation, we propose to conduct a review in 2024 on whether to extend the measures to schemes with below £1 billion in net assets which are not authorised master trusts or an authorised scheme offering collective money purchase benefits, and if so how and on what timescale.

This review would be informed by consideration of TCFD disclosures by occupational pension schemes to-date, their impact, and the availability and quality of both free and paid-for tools and services.

We would propose also to review any regulations and statutory guidance which had been put in place to identify whether any of this needs to be strengthened or updated.

Do you agree with these proposals?

Yes. However, the extension to smaller pension schemes needs to properly consider the costs involved (see our answer to question 12). We also note the reference to "free tools and services", and we caution that whilst something may be free at the point of use, the cost of provision of such services is usually ultimately born by asset owners.

Question 4
We propose that regulations require trustees to:

a) adopt and maintain oversight of climate risks and opportunities
b) establish and maintain processes by which trustees, on an ongoing basis, satisfy themselves that persons managing the scheme, are assessing and managing climate-related risks and opportunities.

We also propose that regulations require trustees to describe:

c) the role of trustees in ensuring oversight of climate-related risks and opportunities
d) the role of those managing the scheme in assessing and managing climate-related risks and opportunities, only insofar as this relates to the scheme itself and the processes by which trustees satisfy themselves that this is being done

We propose that statutory guidance will cover the matters in the box above.

Do you agree with these proposals?

Yes.

Question 5
We propose that regulations require trustees to identify and disclose the climate change risks and opportunities relevant to their scheme over the short, medium and long term, and to assess and describe their impact on their investment and funding strategy.

We propose statutory guidance will cover the matters outlined in the box above.

Do you agree with these proposals?

Yes.

Question 6
We propose that regulations require trustees to assess the resilience of their assets, liabilities and investment strategy and, in the case of defined benefit (DB), funding strategy, as far as they are able, in at least two climate-related scenarios, one of which must be a 2°C or lower scenario and to disclose the results of this assessment.

We propose statutory guidance will cover the matters outlined in the box above.

Do you agree with these proposals?

Yes. We agree that mandatory scenario analysis is a good addition to the general TCFD framework.

Question 7
We propose that regulations require trustees to:

a) adopt and maintain processes for identification, assessment and management of climate-related risks
b) integrate the processes described in a) within the scheme's overall risk management

We also propose the regulations require trustees to disclose:

c) the processes outlined in part a) above

We propose statutory guidance will cover the matters outlined in the box above.

Do you agree with these proposals?

Yes.

Question 8
We propose that regulations require trustees to:

a) select at least one greenhouse gas (GHG) emissions-based metric and at least one non-emissions-based metric to assess the scheme's assets against climate-related risks and opportunities and review the selection on an ongoing basis b) obtain the Scope 1, 2 and 3 GHG emissions of the portfolio, and other non-emissions-based data, as far as they are able c) calculate and disclose metrics (including at least one emissions-based metric and at least one non-emissions-based metric) used to quantify the effects of climate change on the scheme and assess climate-related risks and opportunities

We also propose in regulations that trustees be required to disclose:

d) why the emissions data that is estimated does not cover all asset classes, if this is the case

We propose that trustees will not be mandated to use a specific measure to assess the effects of climate change on the scheme's portfolio.

We propose statutory guidance will cover the matters outlined in the box above.

Do you agree with these proposals?

Yes. We agree that metrics form an important part of TCFD reporting, as this allows comparisons to be made over time. We are less convinced that comparisons between schemes will be possible due to different metrics being used and different data and methodologies being used. However, gathering meaningful data will be difficult for some assets. While there are a number of sources of data for public equities and exchange traded debt, obtaining data for private assets such as real estate and private debt is likely to be problematic.

Question 9
We propose that regulations require trustees to:

a) set at least one target to manage climate-related risks for one of the metrics trustees have chosen to calculate, and to disclose those targets(s)
b) calculate performance against those targets as far as trustees are able and disclose that performance

We propose statutory guidance will cover the matters outlined in the box above.

Do you agree with these proposals?

Yes. We agree with setting targets, as it will motivate actions to improve the metrics.

Question 10
We propose that, for all schemes in scope:

a) the trustees should be required to publish their TCFD report in full on a publicly available website where the report is accessible free of charge
b) the trustees should be required to include in the Annual Report and Accounts a website link to the location where the full TCFD report may be accessed in full
c) the trustees must notify all members to whom they must send the annual benefit statement of the website address where they can locate the full TCFD report – this must be set out in the annual benefit statement
d) the trustees should be required to report the location of their published TCFD report to the Regulator by including the corresponding website address in their scheme return
e) the trustees should also be required to report the location of their published Statement of Investment Principles (SIP), Implementation Statement and excerpts of the Chair's Statement by including the corresponding website address or addresses in their scheme return

Do you agree with these proposals?

Yes.

Question 11
We propose that:

a) The Pensions Regulator (TPR) will have the power to administer discretionary penalties for TCFD reports they deem to be inadequate in meeting the requirements in the regulations
b) there will be no duty on TPR to issue a mandatory penalty, except in instances of total non-compliance where no TCFD report is published

c) in all other respects, we propose to model the compliance measures on the existing penalty regime set out in regulations 26 to 33 of the Occupational Pension Schemes (Charges and Governance) Regulations 2015
d) failure to notify members via the Annual Benefit Statement or to include a link to the TCFD report from the Annual Report will be subject to the existing penalty regime set out in regulation 5 of the Disclosure Regulations

Do you agree with this approach?

We agree that there should be no mandatory fining other than for total non-compliance. However, we are concerned that the discretion could be used in an arbitrary way and/or be seen as a revenue raising mechanism, for example where an infraction was insignificant and the reporting remained within the spirit of the regulations.

Question 12
Do you have any comments on the new regulatory burdens to business and benefits, and wider non-monetised impacts we have estimated and discussed in the draft impact assessment?

We are concerned that the impact assessment significantly underestimates the costs of meeting the proposed requirements. We believe that the costs could be as much as 10x larger than those quoted.

Taking the first year as an example, the total cost is quoted as being some £1.6m for the 103 schemes that are expected to be in scope. This equates to some £15,500 per scheme. There seems to be mismatch between this cost estimate, which assumes a minimum amount of time and resources to prepare a TCFD report, with references in the main consultation materials to the adoption of TCFD reporting as being a journey, with challenges around data availability and in publication and explaining results. If the costed "minimum" approach is adopted, we would expect the resulting TCFD reporting to be of limited value.

There are a various aspects of the costs which we believe are underestimated, for example:

- **On familiarisation, reference is made to there being 30 pages of requirements and guidance to read, whereas these consultation materials run to more than 120 pages, which demonstrates the complexity involved to gain a basic understanding of the subject.**
- **Reference is made to each scheme in scope having on average three trustees. Our scheme has eight trustee directors, and we believe this is typical for the industry, and certainly for large schemes. Further, no allowance is made for trustees refreshing their knowledge each year or for inevitable turnover in trustees.**
- **The hourly wage rates used do not reflect the level of skill and knowledge, and therefore wages of those likely to be involved in preparing and reviewing reports.**

For the avoidance of doubt, as stated in our answers to other questions, we agree with the overall proposal to make TCFD reporting mandatory for pension schemes. We do however believe that the cost estimates used should be consistent with the type and quality of reporting that is required to have the desired impact on asset owner and corporate behaviours.

Question 13
Do you have:

a) any comments on the impact of our proposals on protected groups and how any negative effects may be mitigated?
b) any evidence on existing provision made by trustees in response to requests for information in alternative accessible formats
c) any other comments about any of our proposals?

No.