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Dear Sirs

Response to consultation: Taking action on climate risk: improving governance and reporting by occupational pension schemes

Introduction

Electricity Pensions Trustee Limited ("**EPTL**") welcomes this opportunity to respond to the DWP consultation entitled "**Taking action on climate risk: improving governance and reporting by occupational pension schemes**" (the "**Consultation**"). EPTL is the Scheme Trustee of the Electricity Supply Pension Scheme ("**ESPS**") which is one the largest private sector pension schemes in the United Kingdom, with approximately 166,000 members as at 31 March 2019, of whom approximately 21,000 are active members.

ESPS is an industry-wide pension scheme for non-associated employers within the electricity supply industry. Each non-associated employer has its own Group within ESPS, each Group having its own set of Group Trustees, while EPTL is the Scheme Trustee having certain central functions as set out in the scheme documents of ESPS. Originally, all investment powers were vested in the Scheme Trustee. However, over the years, these powers largely passed to the individual Group Trustees to exercise in relation to assets held for their particular Group (after consulting the relevant Group employers). The Scheme Trustee retains power to invest in assets or funds to which individual Group Trustees wish to subscribe, offering a form of pooled investment within the ESPS for individual Groups. At the moment, the investments made by the Scheme Trustee are limited to forestry. Statements of Investment Principles are maintained by each set of Group Trustees. The Scheme Trustee maintains its own Statement of Investment Principles in respect of the limited investments it makes.

EPTL is responsible for the custody of the assets of the ESPS.

The employers participating in ESPS have a separate body, Electricity Pensions Limited ("**EPL**") to represent their interests. This consultation response is given solely on behalf of EPTL.

General Response

EPTL recognises that the financial risk associated with climate change is an issue of fundamental importance for financial institutions, including pension schemes. As custodians and stewards of our investments, pension scheme trustees need to understand how climate change will impact investment risks and opportunities and build this into our investment beliefs and strategy in an informed and structured way.

EPTL welcomes the approach set out in the Consultation to require larger pension schemes to adopt a structured approach to their governance and reporting in relation to climate change issues by mandatory adoption of TCFD-aligned reporting and the extension of that requirement to smaller schemes over time. The pressing nature of the climate emergency requires that extension to be over as short a period as possible. Cost issues should not be a factor limiting the extension because the requirements promote resilience of investments and returns in the face of the effects of climate change and are therefore in the interests of members, whatever the size of the scheme. There are, however, practical constraints in the availability of reliable data and agreed methodologies for measuring relevant metrics. Government should therefore be proactive in ensuring:

- A common taxonomy and methodology for the identification and measure of greenhouse gas emissions and other metrics relevant to climate change;
- Compulsory adoption by investee companies and asset managers of the TCFD recommendations using that common taxonomy and methodology; and
- Compulsory independent audit of investee bodies' and asset managers TCFD disclosures.

As a final point, the Regulations implementing the principles in the consultation need to address the issue of its application to pension schemes with atypical structures where all investment duties may not be vested in one party. This, of course, includes the ESPS. The only investment managed by EPTL is a specific fund with one narrow asset class (ie forestry). All other investments are managed by the Trustees of the individual Groups. It is important to take account of this distinction in the implementing regulations. It seems appropriate for the party responsible for the statutory Statement of Investment Principles to be responsible for TCFD reporting. This would be the Trustees of the individual Groups in the ESPS, apart from the limited investment managed by EPTL.

Response to questions

We set out the specific questions raised in the consultation and our responses in the Appendix.

We would be happy to have further discussions with you, or to arrange for our advisers to do so, if it would be helpful for us to elaborate any of the above points.

Yours faithfully

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Joanna Matthews, Chair
Electricity Pensions Trustee Limited

Appendix

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?

Answer: We agree that all the above should be included, but do not see the logic of excluding superfunds with less than £1 billion of assets, given that they will have factored compliance issues into their set up costs in their business plans and will be expected to reflect high standards of governance, such that the additional cost of TFCD reporting should be easily absorbable.

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 TCF 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?

Answer: If TCFD reporting is desirable and urgent, which it is, a more demanding timetable for compliance of schemes over £1 billion is appropriate. These schemes have the resources to comply sooner. There may be a practical constraint in the capacity of the adviser market to support earlier adoption, such as by the end of 2022 at the latest, but that was not a concern identified in the Consultation. Another constraint may be the lack of any consistent methodology for companies, investment managers and assets owners to measure and report when adopting TCFD and the difficulty in obtaining data from some companies; however, the pressure of an imminent deadline will help to drive change.

Once a scheme has published a TCFD report, we do not believe it should become exempt from the requirement just because its assets fall below a specified figure. The difficult work is done in putting the structures in place on first adoption of TCFD reporting – it is less onerous to continue reporting and governance structures than to first introduce them. The direction of travel should be one way, and always to extending the reporting requirement.

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?

Answer: We agree that the costs of compliance for small defined contribution schemes may initially be disproportionate, particularly where the costs are borne by the members, and that it makes sense to wait to see how the market develops commoditised products, free and paid-for tools and other services to assist reporting before deciding how to extend the requirements to smaller schemes. However, good governance and good member outcomes are requirements for all defined contribution schemes, regardless of size, and TFCD reporting contributes to both. So the review should be about when to extend the requirements, not whether to extend them.

For all defined benefit schemes and medium to large defined contribution schemes, we think there should be greater ambition and that 2024 should be the deadline for compulsory adoption of TCFD reporting, without requiring any further review.

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?

Answer: We agree with these proposals. While larger schemes may have the necessary expertise in-house to reflect best practice, or will have the resources to engage advisers to assist them, this will not necessarily be the case with smaller schemes where there may be a reluctance to incur professional fees on an exercise which not all trustee boards may be convinced has value. We have seen the value of regulatory prescription and codes of practice in driving best practice in a number of areas for pension schemes and we consider that it has a role in this case. It will help prevent compliance being seen as a box ticking exercise.

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?

Answer: We agree with the proposals. The guidance will help trustees to consider climate change investment issues in a structured way and give a framework for them to challenge their investment managers. As trustee boards will be able to deviate from the guidance, schemes with access to greater expertise and resources who wish to adopt a different approach will be able to do so.

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?

Answer: We agree that modelling the impact of different temperature rises is an important tool in assessing the resilience of an investment strategy to the challenges of climate change; so a requirement for trustees to do so is unobjectionable. However, the Consultation itself recognises the challenges where investee companies do not themselves carry out such modelling and from the variety of assumptions and methodologies used by companies that do. In order for trustees' analysis to be meaningful, Government should drive the adoption of scenario modelling and consistent assumptions and methodologies across industries, rather than allow the pace to be set by companies themselves.

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?

Answer: As with previous answers, we agree with the proposals as a way for helping trustees to think about and manage climate change risk in a structured way.

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?

Answer: In principle, we agree with the proposals for the reasons previously given. However, this is an area where data from investee companies and asset managers is likely to be limited for the chosen metric; and differences in methodologies will add to the difficulty in making consistent and meaningful measurements. The danger in requiring trustees to attempt the process, while recognising the limitations in the data and that it need only be done "as far as they are able", risks this aspect of TCFD reporting becoming a box ticking exercise. It might be better for Government to focus on requiring investee companies and asset managers to provide the data using agreed and consistent methodologies and introduce the required trustee actions at a later date.

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?

Answer: Similar considerations apply as with Question 8.

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?

Is there a better way to notify members of where to find this information?

For example, for DB schemes, might the summary funding statement required by regulation 15 of the Disclosure Regulations be a more appropriate way to signpost members to this information?

Answer: We agree with these proposals. It is important that the full TCFD report be publicly accessible to ensure proper transparency and accountability, but it is appropriate to signpost the location of the report to members, rather than send a full copy to all of them, particularly as some may find such a long and complex document confusing. We also suggest that DB schemes be able to choose the most appropriate method for communicating the location – whether in the annual benefit statement or annual report.

Question 11

We propose that:

(h) 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

(i) 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

(j) 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

(k) 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?

Answer: We agree with this approach.

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?

Answer: We do not have any comments.

Question 13

Do you have:

(l) any comments on the impact of our proposals on protected groups and how any negative effects may be mitigated?

(m) any evidence on existing provision made by trustees in response to requests for information in alternative accessible formats

(n) any other comments about any of our proposals?

Answer: We do not have any further comments.