8 October 2020

Dear Sir/Madam

Taking action on climate risk: improving governance & reporting by occupational pension schemes

The Universities Superannuation Scheme (USS) welcomes the opportunity to respond to the above consultation by DWP and provide below our views on the proposals put forward. In summary, we support, in principle, the proposals to require trustees to address climate risks and opportunities and to disclose these in line with the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD). We recognise that COP26 is an important milestone and support the government's actions to encourage the investment sector and pension funds to address climate change.

Background to USS

Universities Superannuation Scheme (the "Scheme") was established in 1974 as the principal pension scheme for universities and other higher education institutions in the UK. It has more than 400,000 members across more than 350 institutions and is one of the largest pension schemes in the UK, with total fund assets of approximately £68 billion (as at 31 March 2020).

The Scheme's trustee is Universities Superannuation Scheme Limited, a corporate trustee which provides scheme management and trusteeship from its offices based in Liverpool and London in the UK. The trustee company delegates implementation of its investment strategy to a wholly-owned investment management subsidiary company - USS Investment Management Limited - which provides in-house investment management and advisory services. The purpose of the trustee company is to work with higher education employers to build a secure financial future for our members and their families.

As an institutional investor that takes seriously its fiduciary obligations, USS aims to be an active, engaged and responsible steward of the companies and assets in which it invests directly, through its FCA authorised and regulated subsidiary investment manager, USS Investment Management, and through the external asset management services we procure. We devote substantial resources to implementing an active approach towards stewardship and responsible investment across all the scheme's assets – an approach which the trustee company expects both to protect and enhance the value of the scheme's investments in the long-term.

USS's approach towards climate change risk

USS subscribes to the scientific consensus that man-made emissions of carbon dioxide and other greenhouse gases are contributing to changes in the atmosphere that will cause significant changes in global temperatures. While there are uncertainties around the timing of specific impacts, the predicted changes pose a threat to environmental, social and political stability, and to the businesses and other assets in which we invest. It is an issue that could influence our ability to pay the pensions promised and which, as long-term investors, we need to factor into our projections in order to make more informed investment decisions.

USS was among the first pension funds globally to recognise the potential implications of climate change for long-term investors. In 2001, we published an industry leading discussion paper: Climate

Change: a Risk Management Challenge for Institutional Investors. Later that year we co-founded the Institutional Investors Group on Climate Change (IIGCC), which provides a forum for European institutional investors to collectively engage with policymakers on the long-term risks and opportunities of climate change. In the years since, we have demonstrated our leadership on the issue of climate change by constantly advocating for it to be squarely on the agenda of institutional investors.

Climate change, and the policy response to it, also provide investors with opportunities to invest in the transition to a low carbon future. Investing in such opportunities provides the scheme with some resilience against the impacts of a changing climate. The scheme made its first investment dedicated to renewables and clean tech in 2000 and currently has in excess of £1 billion in committed financing to UK renewables.

USS is a longstanding investor in UK onshore and offshore wind and views wind energy as an essential part of the UK's energy mix. Since the formation of the Private Markets Group in 2006, USS has invested over GBP £720m in debt and equity investments in support of the UK wind energy sector and views it as an important part of the UK's zero carbon strategy

USS has currently adopted a range of approaches to integrating climate change into its investment and stewardship process:

- Carbon footprinting
- Scenario analysis
- Portfolio tilt, for example as with our low volatility fund
- Investment in renewable and low carbon Assets
- Divestment from certain thermal coal mining companies
- Engaging with policymakers to encourage them to put in place the regulations that will drive the shift to a low carbon future
- Engagements / stewardship with companies – for example, the scheme is members of CA100+
- Requesting details of how our external managers are addressing climate change
- Membership of / participation in climate related collaborative initiatives (IIGCC, CDP, CA100+)

We have also published a TCFD report and completed the climate change section of the UNPRI reporting and assessment framework (both of which provide public details of our approach to addressing climate change related risks and opportunities).

We provide details of our activities on the USS www site: https://www.uss.co.uk/how-we-invest/responsible-investment

We hope that our response to your consultation will assist in your deliberations and please let us know if we can provide any further information or assistance as you consider the next steps in this process.

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USS's key points on consultation

1. Managing expectations

Whilst we note that the consultation paper requires compliance and reporting by pension funds 'as far as they are able', the proposals create expectations amongst stakeholders that may be difficult to meet in the short term.

The consultation makes clear that the government recognises that asset-based data are required to form the basis of many of the requirements being proposed. Companies are yet to uniformly provide their own TCFD reporting on carbon data, and fund managers are in the same position. As most pension funds are globally diversified, the situation in many markets lags behind where the UK is on climate in general and reporting specifically.

2. Creating an even playing field

As a result, we are unclear as to the logic of requiring larger pension funds to produce TCFD reports when this requirement is not currently in place for asset managers (across asset classes) and indeed underlying assets. As the consultation makes clear, there is a recognition that pension funds will be unable to produce full TCFD reporting as they are reliant on others in the investment chain to provide appropriate data. Even when the TCFD produced its initial guidance, it set its requirements for asset owners, asset managers, and underlying assets at the same time.

We would therefore recommend that The DWP work with other government departments and regulators to align TCFD reporting requirements and frameworks across the investment chain, to ensure that these pension fund requirements can be adequately fulfilled.

3. Annual reporting

We would question whether reporting annually is the correct frequency: Given the long-term nature of both climate change and pension schemes themselves, undertaking full TCFD reporting annually seems excessive as it is unlikely there will be material changes in the short term and would be an expensive exercise to carry out each year for limited benefits.

For example, governance structures are unlikely to (or even should not) change annually, and given the long-term nature of scenarios, the outcome of scenario analysis is not likely to vary over short time periods.

USS would therefore recommend that DWP make full TCFD aligned reporting requirements biannual with intervening annual updates where there is something material to add. The resource required for these kinds of annual updates could then be better spent on stewardship and oversight activities rather than reporting.

4. Metrics and Targets

Similarly, we would question the rationale behind the proposal in paragraph 75 requiring pension funds to obtain quarterly scope 1, 2 and 3 data. Notwithstanding the fact that there is a dearth of scope 3 data available at the present time, the majority of companies and other assets will only be reporting these data annually. Moreover, for many asset classes it will be very difficult to obtain these data in the short and medium term.

This again places a reporting burden on pension funds which is over and above other actors in the investment chain. More importantly, it is not clear the value of requiring such frequent reporting when pension funds should be taking a long-term view of the issue: There has been a general move away from quarterly financial reporting by companies so requiring quarterly reporting in this context seems unnecessary.

In the guidance, we would also recommend that the government clarify the legal basis under which pension funds can set emission reduction-based targets (as outlined in para 78 – "a reduction of 25% by 2030") without fettering trustees' investment discretion.

5. Costs

It is not our experience that implementation of these requirements would cost in the region of £15,000 – indeed, we have incurred much higher costs than this estimate in our undertakings. We would therefore advise that the government should be more realistic in its expectations on cost for pension funds or provide the tools to enable schemes to keep their costs down. e.g. an online scenario analysis tool to support schemes in their undertaking of this part of the process.

6. Pension fund reporting burden

We are concerned that there is an increasing burden on pension funds to report on their sustainability activities for which greater coordination is required among government departments, regulators and industry bodies to ensure there is a more joined up approach with regards to the various requirements and initiatives. We have identified the following (non-exhaustive) current list of sustainability-focussed reporting for pension funds:

- TCFD reporting as per this consultation
- Implementation Statement reporting
- The expectation that pension funds will sign up to the new Stewardship Code with its associated reporting
- EU Sustainable Finance Disclosure Regulation
- UN PRI reporting

7. Guidance needed

It is difficult to comment on the actual implementation of the recommendations being put forward without access to the Guidance referenced in the consultation paper.

8. Clarity re: applicability for hybrid schemes

It is currently unclear whether there will be a requirement for hybrid schemes to provide one or two TCFD reports.

9. Methodology for ITR reporting

We would also question whether the methodology to provide the footprinting required for an Implied Temperature Rise (ITR) exists. Working with other pension funds, USS published a report in 2018 entitled "*If carbon footprinting is the answer what is the question* (https://www.responsible-investor.com/articles/carbon-footprint-piece) highlighting the challenges associated with carbon footprinting of all the asset classes likely to be held by pension funds. More work and guidance are therefore required in this area for ITRs to provide a meaningful and comparative number.