

## DLUHC: Local Government Pensions Scheme (England and Wales): Governance and reporting of climate change risks

Summary of consultation and thoughts on proposed response.

### 1. Governance

New duties on Administering Authorities (AA) to:

- Establish and maintain, on an ongoing basis, oversight of climate related risks and opportunities.
- Establish and maintain processes by which they can, on an ongoing basis, satisfy themselves that those who undertake climate-related governance activities, advisors, and those who assist the AA (including officers and advisors) with respect to climate related governance are doing so effectively.

#### Question 1: Do you agree with our proposed requirements in relation to governance?

- *As investment strategy is the responsibility of scheme manager (AA) sensible that responsibility for climate risk and opportunities sits there too.*
- *However, need clear guidance on governance role where there could be tension between pools and AA in terms of setting targets.*
- *Knowledge and understanding of all involved? committee are NOT experts, neither are officers.*
- *“properly qualified advisers” – how identified and assured of qualification?*
- *Technical advice that is accessible – how?*
- *Bringing in additional expertise where necessary – from where? additional cost?*
- *Acknowledgement of time and capacity constraints (IW is one of 8 LGPS funds with assets less than £1bn).*
- *Officers, advisers and pool will need to provide advice ... How is effectiveness to be measured?*
- *Duty on AA as a whole, not individual officers, advisers or pool. Needs to be documented in constitution/terms of reference/scheme of delegations. Officer job descriptions. Adviser contract specification.*
- *Welcome statutory guidance from DLUHC on this matter.*

### 2. Strategy

New duties on AAs to:

- Identify, on an ongoing basis, climate-related risks and opportunities that will impact the investment and funding strategy of the AA, over the short, medium and long term.
- Assess, on an ongoing basis, the impact of identified risks and opportunities on the AA's investment and funding strategy.

#### Question 2: Do you agree with our proposed requirements in relation to strategy?

- *Agree can't separate investment strategy from funding strategy, so impact of risks need to be considered on both equally.*
- *The new valuation climate scenario analysis will go some way to fulfilling TCFD requirements but would want to maximise the effectiveness of the fund actuary analysis by getting it to include as many TCFD requirements as possible for resource reasons*
- *Requires a quite detailed understanding of the issues to be held at some level in the governance/management structure.*
- *Knowledge and understanding of all involved? Carbon pricing?*
- *Welcome statutory guidance from DLUHC on identification of risks and opportunities, impact assessment and factors to be taken into account.*

### 3. Scenario analysis

New duty on AAs to:

- Assess their assets, liabilities, investment strategy and funding strategy against climate risks and opportunities in at least two climate scenarios. This assessment must include at least one scenario based on a global temperature rise of 2°C or lower on pre-industrial levels. This assessment must occur at least once every valuation cycle. In interim years, AAs must consider whether any changes in the fund have been substantial enough to require scenario analysis to be repeated.

#### Question 3: Do you agree with our suggested requirements in relation to scenario analysis?

- *Credible, distinctive and relevant scenarios ...?*
- *Grateful for proviso “as far as they are able”.*
- *qualitative or quantitative analysis – quantitative where data available, and more data asap.*
- *Welcome statutory guidance on scenario analysis and dealing with barriers to information.*
- *Two or more scenarios ... at least one of which must be 2°C or lower – potentially significant extra work for officers and additional cost of advisers/modelling.*
- *Agree that scenario modelling should be done as part of the valuation cycle, once every three years – timing to be considered as part of business planning.*
- *What is classed as “substantial change to the fund” to require revision of scenario analysis? potential for different definitions.*

### 4. Risk Management

AAs to:

- Establish and maintain processes for the purpose of enabling them to identify and assess climate-related risks.
- Establish and maintain processes for the purpose of enabling them to effectively manage climate-related risks.
- Ensure, on an ongoing basis, climate-related risks management processes are integrated into their overall risk management.

#### Question 4: Do you agree with our proposed requirements in relation to risk management?

- *Important that climate risk management is embedded in overall risk management processes, not seen as a separate exercise.*
- *Knowledge and understanding of all involved?*
- *Capacity to identify, assess and take action on risks and opportunities?*
- *Welcome statutory guidance from DLUHC on processes, factors to consider and types of risk and opportunity.*

### 5. Metrics

AAs to calculate and report on the following metrics:

- Metric 1 (absolute emissions metric) – Total Carbon Emission, which includes the Scope 1, 2 and 3 emissions reported separately, as well as the sum of the three.
- Metric 2 (emissions intensity metric) – Carbon Footprint. This is Carbon Emissions divided by the total assets of the fund to which the data relates. It should be calculated separately for Scope 1, Scope 2 and Scope 3 emissions.
- Metric 3 (data quality metric) – the percentage of assets for which Scope 1, 2 and 3 emissions are verified, reported, estimated or unavailable, in line with the GHG Protocol.
- Metric 4 (Paris alignment metric) – the percentage of the fund’s assets for which a public Paris aligned commitment has been made, i.e. net zero by 2050.

Recommend in statutory guidance that AAs consider whether they wish to calculate any other climate related metrics recommended by the TCFD in order to inform assessment of climate risks.

**Question 5: Do you agree with our proposed requirements in relation to metrics?**

- *Important that consistent metrics are reported by individual fund through time, to measure progress.*
- *Consistency between AA is important to allow comparability – however concern that this will lead to “league tables” and criticism of lower scores.*
- *Must recognise that there is difficulty with metrics as there is inconsistent data in asset classes other than equity*
- *Agree that metrics should be defined in statutory guidance rather than regulations, to allow ease of update as situation changes.*

**Absolute emissions**

- *Agree that excluding scope 3 emissions could present a misleading picture, particularly in some sectors.*
- *Although concern about the volume of information reported, fair to report scope 1, 2 and 3 separately and together for absolute emissions, to ensure clarity (particularly as Scope 3 is more uncertain).*
- *Welcome inclusion of the appropriate methodology for calculation of absolute emissions in guidance. Although concern that not all investment managers/companies will use that particular methodology -consequences if they don't?*
- *Concern that giving the option to report at investment level as well as at whole fund level will provoke negative reaction to those funds that don't/can't report at investment level.*

**Emissions intensity**

- *Required to be reported separately for each scope (para 77) but then propose that only the top-level figure at whole fund level is reported (para 79) – is this contradictory?*
- *Not sure why a fund would not be able to produce the required Carbon Footprint metric. If option for Weighted Average Carbon Intensity is given, how will a Scheme-wide figure for this metric be calculated and/reported?*

**Data quality**

- *Concern that there is an expectation that the LGPS “can play its part in increasing data availability and quality”. Principle objective of LGPS is to pay benefits to its members – cannot afford to divert significant resource away from this purpose.*
- *Will AA be criticised if its data quality “score” is lower than others?*
- *Verified and reported – independent third party – of the investment manager/company or the reporting authority? Could there be an issue of third party reliance limitations?*
- *Complexity in reporting for % of verified, reported, estimated or unavailable separately for each scope ... accuracy of information input and comprehension of output.*
- *Additional cost for use of third parties to provide/analyse information? Availability of these third parties? And verification of expertise? And significant extra work for officers in consolidating information.*

**Paris alignment**

- *Agree that binary target measure is most appropriate for LGPS*
- *Concern that there will be increasing pressure to enforce other metrics, which not every fund may have capacity to deliver.*
- *Would request caution in government changing its approach to required reporting – time will be needed to implement different data collection/reporting methodologies.*

**6. Targets**

- *AAs must set a target for their fund in relation to one of the metrics which they have selected. The target may be in relation to one of the mandatory metrics (absolute emissions, emissions intensity, data quality or Paris alignment), or any other climate-related metric endorsed by the TCFD which the AA choses.*

- AAs must annually measure, as far as they are able, the performance of their fund against the target they have set and taking into account that performance, determine whether the target should be retained or replaced.

There is no expectation that AAs should set targets which require them to divest or invest in a given way, and the targets are not legally binding.

**Question 6: Do you agree with our proposed requirements in relation to targets?**

- *Grateful that requirement is for a target against only one of the metrics.*
- *Very clear that no requirement for divestment/investment – AA is sovereign when it comes to investment strategy.*

**7. Annual climate risk report**

- AA must publish a Climate Risk Report every year, at the same time as the AA's annual report is published.
- Climate Risk Report must be accessible to two distinct types of user: specialist and non-specialist.

Content set out at end of this report.

**Question 7: Do you agree with our approach to reporting?**

- *Acknowledge "comply or explain" requirement of 'as far as they are able' statement – reasonable and proportionate steps given costs and time constraints – not looking for excuses not to comply!*
- *Suggest that Climate Risk Report should be separate from Annual Report – Annual Report already cumbersome and not very user-friendly, adding this additional, very complex, element will make it worse, and detract from usefulness/accessibility of Climate Risk Report.*
- *Scenario analysis must be carried out in 2023/24 – capacity issues for advisers to support this? Does this allow sufficient time for officers/committees/boards to obtain sufficient knowledge and understanding to understand the process and the results?*
- *"AAs should explain in their Climate Risk Report whether they have carried out a new analysis, and if not give a short explanation as to why". As only required once every three years unless significant change, will this be acceptable reason?*
- *Concern over complexity of reporting needs with proposal for 'simplified' executive summary for the lay-reader and "technical in content and dense with information" main body. Do officers at AAs have the skills/knowledge/understanding to provide both forms of report, and how to ensure that each section is consistent with the other and understandable by the relevant audience?*
- *Level of time, cost and effort put in compared to number of readers??*
- *No issue with publication on scheme website and informing members that it is available.*
- *Requirement to notify members that report is available with issuance of ABS is inappropriate – ABS deadline is 31 August each year, so either 3 months before report is due OR 9 months after it was published.*

**8. Scheme climate risk report**

- In addition to individual climate risk reports, an annual Scheme Climate Risk Report to be produced by Scheme Advisory Board.

**Question 8: Do you agree with our proposals on the Scheme Climate Risk Report?**

- *Agree scheme-wide report should show aggregated data for the whole scheme across metrics.*
- *Agree that links to individual AA reports should be provided on the SAB website.*
- *Concern that publication of metrics for each individual AA in Scheme Climate Risk Report will result in league tables and inevitable comparison between authorities – potential for funds to be labelled as "worst performing" generating unnecessary criticism and reputational damage.*

<ul style="list-style-type: none"> <li>• <i>There needs to be consistent definitions and methodologies, some asset classes are less developed in reporting so a change in asset allocation can mean an “improvement” or “decline” merely from changing reporting regimes</i></li> <li>• <i>Although clearly states no expectation from government that AAs should divest, there is a real danger that pressure groups may use the information in the report to target individual AAs.</i></li> <li>• <i>Probably at this level that the data quality metric could be used to increase pressure on industry to improve standards.</i></li> </ul>
<p><b>9. The role of LGPS asset pools</b></p> <ul style="list-style-type: none"> <li>• For pooled assets, expect that the pools will be able to provide data, calculate metrics and carry out scenario analysis on those assets where data is available.</li> </ul>
<p><b>Question 9: Do you have any comments on the role of the LGPS asset pools in delivering the requirements?</b></p> <ul style="list-style-type: none"> <li>• <i>Efficiency expected from pool providing reports on all pooled investments which can be utilised by all AAs invested.</i></li> <li>• <i>Concern that guidance seems to suggest that AAs can become more efficient by aligning their investment strategies with the pool – AA is, and must remain, sovereign when it comes to setting investment strategy; pool is there to facilitate that strategy.</i></li> <li>• <i>Benefit to all AAs to discuss their thinking re metrics, targets and scenarios with others in same pool, but remembering that each AA has individual responsibility for determining their own criteria and reporting etc.</i></li> </ul>
<p><b>10. Guidance and reporting template</b></p> <ul style="list-style-type: none"> <li>• DLUHC provide high level statutory guidance – including governance activities required of AAs and the Climate Risk Report.</li> <li>• SAB to produce more detailed operational guidance.</li> <li>• SAB asked to produce a standard template which AAs will be required to follow in producing the Climate Risk Report.</li> </ul>
<p><b>Question 10: Do you agree with our proposed approach to guidance?</b></p> <ul style="list-style-type: none"> <li>• <i>Need to ensure all areas where guidance is promised elsewhere in consultation is included in whatever is provided: governance, strategy, scenario analysis, risk management, annual report.</i></li> <li>• <i>Detailed operational guidance by SAB is welcomed – drafted by those who understand the scheme.</i></li> <li>• <i>Standard template welcomed to ensure comprehensive and consistent reporting across the LGPS; acknowledging risk that this may result in some generic responses rather than AA specific.</i></li> </ul>
<p><b>11. Knowledge, skills and advice</b></p> <ul style="list-style-type: none"> <li>• Not imposing any legal requirements on an individual’s knowledge and skills ... base knowledge regarding climate risks will be necessary in order to ... interpret the results of scenario analysis.</li> <li>• AAs must take proper advice regarding assessing and managing climate risks.</li> <li>• AAs need to satisfy themselves that the advice is high quality and provided by appropriately qualified people.</li> </ul>
<p><b>Question 11: Do you agree with our proposed approach to knowledge, skills and advice?</b></p> <ul style="list-style-type: none"> <li>• <i>May be beneficial to require a minimum level of knowledge and understanding for those responsible for preparing and reviewing the Climate Risk Report ... perhaps some recommended qualifications?</i></li> </ul>

- *SAB should work with CIPFA to include learning requirements in any new Knowledge and Skills Frameworks, and/or work with industry experts in developing a learning package relevant to this requirement?*
- *Could TPR develop a learning module for trustee toolkit on climate risk reporting considerations?*
- *Could SAB work to provide a list of recognised advisory firms for this purpose? Possibly a National LGPS Framework-type approved suppliers list?*
- *How will AAs be expected to verify that advice is of high quality and provided by appropriately qualified people? Especially as many may not be completely sure of the advice they are looking for.*
- *Potential for capacity issues in supply market for these appropriately qualified, high quality advisers? Possible cost pressures on those who may be “late to the party”?*
- *Pools could provide development sessions for their AA members in respect of data gathered for the pooled investments, explaining the modelling undertaken in scenario analysis and interpretation of those results?*

## **12. Impact on protected groups**

- Initial assessment – no impact on any of the protected groups.

**Question 12: Do you have any comments on the impact of our proposals on protected groups and on how any negative impacts may be mitigated?**

- *No comments.*

Climate Risk Report must include the following information:

Area	Disclosure Requirement
Governance	<p>Describe the AA's oversight of climate-related risks and opportunities</p> <p>Describe the role of any person other than the scheme manager who undertakes relevant governance activities and the process by which the committee satisfy themselves that this is being done</p> <p>Describe the role of any person who (other than a legal advisor) advises the scheme manager on relevant governance activities and the process by which the committee satisfies itself that adequate steps are being taken</p>
Strategy	<p>Describe the climate-related risks and opportunities which the scheme manager has identified</p> <p>Describe the scheme manager's definition of short term, medium term and long term</p>
Scenario Analysis	<p>Describe the most recent scenarios the scheme manager has analysed</p> <p>Describe the impact of the climate-related risks and opportunities on the AA's investment and funding strategies</p> <p>Describe the potential impacts on the AA's assets and liabilities which the AA has identified in the most recent scenarios and the reason for any data which is missing from the analysis</p> <p>Describe the resilience of the AA's investment and funding strategies in the most recent scenarios the AAs have analysed</p>
Risk Management	<p>Describe the processes which the AA has established for identifying and assessing climate-related risks to their fund</p> <p>Describe the processes which the AA has established for managing climate-related risks to the AA</p> <p>Describe how these processes are integrated into the AA's overall risk management</p>
Metrics	<p>Report the metrics which the AA has calculated (or an explanation as to why these were not possible to calculate)</p>
Targets	<p>Report the target which the AAs have set and the performance of the AA against that target.</p>