

BLOG: A five-step climate action plan for pension funds

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This blog by Charlotte Tyrwhitt-Drake is part of a weekly series from the Pensions for Purpose team.

Climate change presents both risks and opportunities for all of us, including pension funds. Impetus is building with the Pension Schemes Bill, requiring pension scheme trustees to fully consider and disclose their climate-related financial risks and opportunities in line with recommendations by the Task Force on Climate-related Financial Disclosures (TCFD), now going for Royal Assent. This is no longer a "nice to have", it is fundamental to ensuring all members benefits can be paid (including the last member) and that they can spend that money in a world worth living in.

Karen Shackleton, Chair, has been working with pension funds through workshops and roundtables on how a pension fund can take action on climate change. The most recent roundtable we held on this with **Richard Butcher, Chair at the PLSA and Managing Director at PTL**, was oversubscribed and focused on:

- a) the challenges in approaching climate change, such as the lack of clarity on terms of reference and lack of a universal language, lack of expertise in the industry, lack of green products and the need for a coherent narrative.
- b) the **five steps pension funds can take**, representing a clear process for making progress:
 1. Clarify your investment beliefs;
 2. Carry out a baseline assessment of your portfolio;
 3. Undertake an investment strategy review;
 4. Focus on key questions when selecting managers; and
 5. Monitor and review the impact.

We had a very interactive session with trustees of pension schemes asking some key questions:

- How can we access advice and mapping on sustainability and specifically the UN Sustainable Development Goals?

These are very pertinent questions, especially given the concern around a lack of expertise. Pensions for Purpose finalised an SDG mapping report last year and found varied outcomes (some were mapping more SDGs than others and to different levels of granularity), although there are advisers out there that can offer this service, and which are being used by pension funds.

- What about the role of the Local Government Pensions Scheme pools - could they be doing more to educate others on climate change, as well as creating consistency?

Certainly, there appears to be evidence that this is happening to varying degrees with different pools, but it is not a uniform approach.

- How long will it take to get a green taxonomy?

The government announced last year that they were embarking on a common framework for determining which activities can be defined as environmentally sustainable based on the work on the EU taxonomy but also drawing on the expertise a UK Green Technical Advisory Group. With COP26 coming in the Autumn, it seems likely that progress on this may be made before then.

- Are members views being taken into account?

Now, this was one of the more contentious areas of discussion with several different views on how effective member engagement is, particularly in relation to defined benefit schemes. Some argued that it is still difficult and a very protracted process to engage members, leading to unintended consequences which may not be in the best interests of the scheme; others argued that climate change made it more likely members would engage with their pension and therefore be active, as well as the fact that the pension has a responsibility for every member, including their youngest members, who were more likely to be affected by climate change.

- Effective stewardship is key, but many pension schemes are invested in pooled funds, so how can we address this?

Institutional investors in pooled funds have historically relied on the investment manager to execute a voting policy for the pooled fund. When their preferences have diverged from the manager's policy, they have been forced to accept the votes placed by the manager. There are current changes under way to change this, driven by initiatives from the Department for Work and Pensions and the Association for Member Nominated Trustees. Just last week it was announced that Asset Management Exchange (AMX) and asset manager DWS had joined forces to develop an investment service that allows pension schemes to express their stewardship preferences in pooled funds.

- How do we encourage engagement, not simply divesting?

Divesting should be an absolute last option following engagement. The economy of the future needs to take everyone with it and we are seeing the positive influence of engagement. Climate Action 100+ has achieved a considerable amount of success in pushing large companies to shift their strategies on climate change.

- How are we going to get to carbon neutral – will we need to rely on offsetting?

The reality may well be that some offsetting is required early on to reach carbon targets, but it should not be an end in and of itself. The primary goal should be to invest in solutions and to use stewardship as a form of offsetting (engagement with companies leading to reduced emissions). We also must factor in all of the issues which lead to climate change, e.g. biodiversity loss, irresponsible mass consumption, undervaluing natural capital. The key is to be clear on the how, what and why of what you are doing to get to your target.

We explored a significant and wide-ranging group of topics on climate change in a peer-to-peer network and had a rich discussion which will catalyse change. If you would like to join us for another of these events and/or be part of our member forum on Paris Alignment/TCFD, please get in touch with Karen Shackleton – karen.shackleton@pensionsforpurpose.com.

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