7th October, 2020

Climate Governance & ESG Team
Department for Work & Pensions
Caxton House
Tothill Street
London
SW1H 9NA

Submitted By Email to: pensions.governance@dwp.gov.uk

Dear Ms. Livesey, Mr. Rhodes, Mr. Blair and Mr Farrar,

CFA UK Response to DWP's Consultation - Taking action on climate risk: improving governance & reporting by occupational pension schemes

The CFA Society of the UK (CFA UK) is pleased to respond to this consultation from the Department of Work & Pensions ("DWP").

CFA UK is the professional body that serves nearly 12,000 leading members of the UK investment profession. Many of our members work with pension funds, either managing investment portfolios, advising on investments or as an in-house employee responsible for pension investment oversight[1].

Climate Change and wider ESG issues are of great and growing importance to CFA UK's members and our umbrella organisation, CFA Institute. It is clear that if capital is to be allocated in a way that fully reflects climate change risks and broader ESG issues then better disclosures by investees, and in turn asset managers and pensions schemes, are of paramount importance. These disclosures need to be both (i) supported by proper data and (ii) enjoy common appreciation and understanding within the investment profession, investees and investors. Unless this occurs, climate change risk and ESG risks will continue to be either not reported on, inadequately reported on or even misreported; and as a consequence investors' capital will continue to be allocated in a way that does not correctly reflect the risks that climate change and ESG factors bring to companies and investments in them. There are few investment arenas where this is more true than in pensions, with its long-term investment horizons out to 2050 and beyond.

Out of necessity the investment world is undergoing a major transformation in a drive to measure, analyse, understand and respond to climate change and ESG risks. CFA UK and CFA Institute are playing their part in this:

- CFA UK last year launched its Certificate in ESG Investing[2]. More than 2,500 individuals (around 75% from the UK) have registered for the exam.

---

1 More details on CFA UK and the CFA Institute are provided in Appendix I.

2 CFA UK Certificate in ESG Investing (https://www.cfauk.org/study/esg#gsc.tab=0)

- CFA UK is also investigating the launch of a similar qualification specifically on the issue of climate change in investment;
- CFA Institute is currently consulting on a set of ESG Standards for Investment Products. These Standards aim to provide a common global framework by which the ESG focus and/or activities of all pooled investment vehicles will be described to end investors and other stakeholders in standard and universal terms[3];
- CFA UK advocates widely on stewardship, ESG and climate change issues[4]. CFA UK most recently submitted a response to the FCA on the important and closely related issue of company climate change disclosures and reporting[5].

We applaud the ambition of the DWP's consultation's proposals - and indeed in some of our answers advocate for even more ambitious targets. At the same time, however, we would stress the scale of the transformation required in the infrastructure of both corporate and investment reporting. In a recent survey of our members[6], 82 per cent of respondents found the lack of reliable data and metrics to be a challenge in integrating climate considerations into investment decision-making.

We have provided detailed answers to the first twelve questions within your consultation and these can be found in Appendix III. However, CFA UK would like to highlight the following points which resonate through our answers to the individual questions:

- Firstly, it is imperitive that these new reporting requirements on pension funds are applied with consistency to encourage peer accountability. This means:
    - Both defined benefit and defined contribution schemes need to report using a common set of metrics and at least one of these must be a prescribed quantitative metric.
    - TPR must develop a harmonised reporting template. This should then allow comparability between schemes and bring essential transparency and meaning to these new reporting obligations.
    - TPR should also establish a web-portal where these reports can be publicly accessed and ideally conduct an aggregation exercise and possibly an index against which individual schemes' reports can be compared.
    - This consistency would also mean that trustees could then set target carbon objectives for their scheme informed by peer group comparison.
    - These targets could be open to change, should international bodies e.g. TCFD decide that it was required; a case in point would be potentially a rising bar over time if global warming continued on its current path.

[3] CFA Institute consultation paper on the development of ESG Disclosure Standards for Investment Products: (https://www.cfainstitute.org/-/media/documents/code/esg-standards/consultation-paper-on-esg-disclosure-standards.ashx)
[4] A list of our recent consultation responses in these areas is provided in Appendix II.
[5] CFA UK Response Letter to the FCA re: CP 20/3 (https://www.cfauk.org/-/media/files/pdf/pdf/5-professionalism/2-advocacy/responses/ccdr-final-letter-to-fca.pdf)

[6] CFA UK conducted two surveys: (i) a full membership survey (https://www.surveymonkey.com/results/SM-QB27S8GG7/), sent to the entire membership of CFA UK, on the broad topic of climate change and investment, which received 330 full or partial responses, and (ii) an expert group survey (https://www.surveymonkey.com/results/SM-GN7HGM8B7/), which canvassed a subset of the membership survey sample composed of members willing to volunteer for our advocacy work on climate change disclosure. This second survey received 49 responses.

N.B. Please consider the make-up and sample size of these cohorts when reviewing the results we cite.

- Secondly, in relation to the scenario reporting. CFA UK believes schemes should be required to publish a scenario based on the Paris target ('Base Case') and in addition one more extreme but plausible scenario ('Extreme Case'). This would allow trustees and members to compare outcomes.

- Thirdly, the requirements should apply to the broadest possible scope of asset owners. It could be self-defeating if this regulation allowed certain asset owners to avoid reporting by reconstituting themselves in a way that meant they were not required to comply. By extension all asset classes need to be in scope. Assets outsourced to insurers should be included in schemes' reports. Every encouragement should be given to allow for more complex or difficult assets to be included (e.g. property, derivatives, sovereign bonds (including gilts), cash). Perhaps these assets should be the focus of a subsequent consultation. Where a scheme does not comply and excludes certain assets from its report, an explanation should be forthcoming.

- Fourthly, schemes' reporting needs to be both easily accessible on their web-site (and TPR's website, as stated above) as well as timely. CFA UK would advocate being in favour of rising fines for progressively late reporting.

We would like to thank you for the well-prepared, well-targeted and infomative consultation paper. We hope you find our reponses useful. Please do let us know if you would like you discuss our views in more detail.

Yours sincerely,

Will Goodhart,
Chief Executive
CFA Society of the UK

Andrew Burton
Professionalism Adviser
CFA Society of the UK

With thanks to contributions from the CFA UK Pensions Expert Panel and the [CFA UK Professionalism Steering Committee]

Appendix I: About CFA UK & the CFA Institute

CFA UK: serves nearly 12,000 leading members of the UK investment profession. Many of our members work with pension funds, either managing investment portfolios, advising on investments or as an in house employee responsible for pension investment oversight.

- The mission of CFA UK is to build a better investment profession and to do this through the promotion of the highest standards of ethics, education and professional excellence in order to serve society's best interests.

- Founded in 1955, CFA UK is one of the largest member societies of CFA Institute (see below) and provides continuing education, advocacy, information and career support on behalf of its members.

- Most CFA UK members have earned the Chartered Financial Analyst® (CFA®) designation, or are candidates registered in CFA Institute's CFA Program. Both members and candidates attest to adhere to CFA Institute's Code of Ethics and Standards of Professional Conduct.

- For more information, visit www.cfauk.org or follow us on Twitter @cfauk and on LinkedIn.com/company/cfa-uk/.

CFA Institute: is the global association for investment professionals that sets the standard for professional excellence and credentials.

- The organization is a champion of ethical behavior in investment markets and a respected source of knowledge in the global financial community. Our aim is to create an environment where investors' interests come first, markets function at their best, and economies grow.

- It awards the Chartered Financial Analyst® (CFA), and Certificate in Investment Performance Measurement® (CIPM) designations worldwide; publishes research; conducts professional development programs; and sets voluntary, ethics-based professional and performance-reporting standards for the investment industry.

- CFA Institute has members in 162 markets, of which more than 170,000 hold the Chartered Financial Analyst® (CFA) designation. CFA Institute has nine offices worldwide and there are 158 local member societies.

- For more information, visit www.cfainstitute.org or follow us on Twitter at @CFAInstitute and on Facebook.com/CFAInstitute.

APPENDIX II: Recent CFA UK response letters on stewardship, ESG and green finance issues

Response to the FCA consultation (CP20/3): proposals to enhance climate-related disclosures by listed issuers and clarification of existing disclosure obligations
[NOT YET FILED]

Response to the BSI (PAS7341) 'Responsible and Sustainable Investment'
(February 2020)
<link to file from CFA UK>

Response to the FCA consultation (CP19/15) 'IGCs: Extension of Remit'
(July 2019)
<link to file from CFA UK>

Response to the FRC and FCA joint discussion paper (DP19/1) 'Building a regulatory framework for effective stewardship'
(April 2019)
<link to file from CFA UK>

Response to FRC's consultation on the proposed revision to the Stewardship Code (March 2019)
<link to file from CFA UK>

Response to FCA consultation CP19/07 on proposals to improve shareholder engagement
(March 2019)
<link to file from CFA UK>

Response to the Investment Association's consultation on sustainability and responsible investment
(March 2019)
<link to file from CFA UK>

Response to FCA Discussion Paper (DP18-08) on Climate Change and Green Finance
(January 2019)
<link to file from CFA UK>

Response to FRC's consultation on proposed revisions to the UK Corporate Governance Code and the future direction of the Stewardship Code
(Feb 2018)
<link to file from CFA UK>

Appendix III: Responses to Questions

***Q1:* 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?

CFA UK agrees with the policy proposals (1a-1c) and would recommend the following:

i) Expanding the scope to include trust schemes with more than GBP 500m in assets that have invested assets using commingled vehicles, who may be helped by TCFD reporting provided by the respective asset managers of the commingled vehicles.

ii) Expanding the scope to include trust schemes whose assets are managed by providers of Fiduciary Services, whose assets are in excess of GBP 500m, who may be helped by TCFD reporting provided by the respective providers of those Fiduciary Services.

iii) To accurately employ the TCFD implementation methodology of "comply" or "explain" across different asset classes, we would request further guidance and metrics to ensure practical and cross-comparable implementation of TCFD across schemes so as to reduce ambiguity. We also believe that this will allow the true scope of assets covered by TCFD reporting to be reported.

We believe that the criteria for scope should be expanded as outlined above as CFA UK is entirely supportive of achieving the greatest coverage for TCFD reporting within the shortest period of time.

Pension schemes with assets lower than the suggested threshold may still be in a position to provide detailed TCFD reporting if they have outsourced their investment decision making to a Fiduciary Service provider, who may in aggregate have assets under management which would be above the suggested minimum thresholds. TCFD reporting would then be possible as this exercise would be carried out by the Fiduciary Service Provider and shared with the pension scheme. This would allow for greater coverage of scheme assets without placing an additional administrative burden on schemes with lower asset sizes.

In relation to the scope as detailed above, we would also ask that it be broad enough to account for changes in market structure over time; we envisage in particular consolidation taking place between schemes, and see Defined Contribution schemes replacing Defined Benefit schemes to become the dominant structures over time. We also believe that the inclusion of Mastertrusts and Collective Defined Contribution schemes are important and will continue to play a greater role in the future of scheme structures.

We would also point out that the possibility of "comply" or "explain" within TCFD reporting, while practical, also gives rise to opportunities to deviate from disclosure requirements across assets. As processes and methodologies for implementing TCFD reporting are still being honed, we would encourage a more active participation from the proposals in guiding, in general terms, which assets would be reasonably be expected to included within TCFD reporting under normal circumstances. While corporate equity and corporate credit holdings are easier to detail under TCFD reporting, other commonly held pension asset classes give rise to greater complexity and ambiguity. We believe that pension assets including property, private credit, cash, derivatives and gilts will not be readily carbon assessed in the same way equity and credit portfolios currently are by asset managers. This provides an additional challenges to TCFD reporting. One important example would be UK gilts, which are held actively across practically all schemes, and the expectation of whether this would constitute "comply" or "explain" under normal circumstances. We are also sceptical that asset managers will be fully prepared for the implementation of the EU taxonomy at the fund level by Q4, 2020.

We note that while the DWP may not be able to place a direct regulatory onus on the providers of fiduciary services and commingled funds, we would recommend that activities be co-ordinated as far as possible between different parties - e.g. FCA when looking to achieve climate related governance across pension schemes.

We believe that additional guidance to that detailed in the proposals as to which assets would under normal circumstances reasonably be expected to be included within TCFD reporting, would provide a common expectation on trustees and service providers in their TCFD reporting roles. Ultimately this would lead to greater uniformity and comparable reporting across schemes.

Finally, we believe that this will allow the "true" scope of assets captured by TCFD reporting to be ascertained.

***Q2:* 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?

CFA UK are not in favour of the proposals (2a-2g) and would make the following comments:

i) Multiple criteria and differing deadlines for scope definition and implementation would create unnecessary challenges and potentially cause confusion; we would recommend dramatically simplifying as far as possible the scope and deadlines for implementation, ideally with a single date for implementation and accountability across schemes.

ii) TCFD recommendations were originally made in 2017, with an envisaged 5-year plan to implement as was practically possible. We appreciate that there may be practical challenges for the adoption of an aggressive timeline - e.g. working with service providers who will be delivering necessary inputs for the assessment; however, we believe that schemes should be prepared to adopt TCFD at the earliest opportunity.

CFA UK believe that simplification of the proposals to a single date of implementation would be in the best interests of all concerned in the value chain tasked with implementation of TCFD reporting. This would ensure that trustees, fiduciary service providers, asset managers and internal teams and processes would be aligned to a simplified delivery schedule. We highlight that both asset managers and fiduciary service providers deal with multiple schemes and so the added complexity of providing the necessary TCFD inputs for specific schemes may prove to be challenging when compared with a simplified overall implementation schedule for schemes.

We also note that TCFD reporting may be one of many of regulatory changes which will be impacting schemes and trustees, each of which will require additional resources to properly manage; as such simplification of the proposed implementation would aid in minimizing drawing on limited schemes' resources.

As shared in our response to the proposals outlined in question 1., by expanding the scope for scheme inclusion as detailed previously, we believe it would be easier to catalyse a faster adoption across schemes of TCFD reporting.

We would also advocate implementation at the earliest opportunity, following the tentative 5-year path towards implementation shared by the TCFD in 2017. While we believe this to be an aggressive timeline for adoption, we would ask that the proposals encompass the need for asset managers and service providers to be key delivery partners of inputs required for TCFD disclosure so as to: i) catalyse the adoption of TCFD reporting across schemes; and ii) minimize the additional resources on the part of schemes in meeting TCFD disclosures. In this regard we note that TCFD is global in nature and that should be used to encourage overseas asset managers as well as UK asset managers to embrace this process.

Finally, we highlight the need for co-ordinated regulatory activity. If successful and meaningful metrics are to be delivered, it is imperative that both asset managers and fiduciary services providers are tasked with similar requirements to those of pensions schemes trustees. We note that the current scope of FCA CP10/3 will not be broad enough to be effective in meeting the requirements on the part of pension fund trustees for TCFD reporting.

***Q3:* 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?

CFA UK agrees with the proposals, albeit with the caveat of referring to our response to Question 1 in relation to to the scope of schemes to be included within the proposals. For completeness, these are shared again below:

i) Expanding the scope to include trust schemes with more than GBP 500m in assets that have invested assets using commingled vehicles who may be helped by TCFD reporting provided by the respective asset managers of the commingled vehicles.

ii) Expanding the scope to include trust schemes whose assets are managed by providers of Fiduciary Services, whose assets are in excess of GBP 500m, who may be helped with TCFD reporting by respective providers of those Fiduciary Services.

iii) For all schemes falling outside of the scope as detailed earlier in question 1 and stated above, we would agree with a review conducted in 2024 as stipulated above.

Our rationale as shared earlier in our answer to question 1 is as follows:

We believe that the criteria for scope should be expanded as outlined above as CFA UK is entirely supportive of achieving the greatest coverage for TCFD reporting within the shortest period of time.

Pension schemes with assets lower than the suggested threshold may still be in a position to provide detailed TCFD disclosures if they have outsourced their investment decision making to a Fiduciary Service provider, who may in aggregate have assets under management which would be above the suggested minimum thresholds. TCFD reporting would then be possible as this exercise would be carried out by the fiduciary service provider and shared with the pension scheme. This would allow for greater coverage of scheme assets without placing an additional administrative burden on schemes with lower asset sizes.

***Q4:* 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?

While CFA UK agrees with the proposals (4a-4d), we would however, make the following comments:

i) CFA UK would caution against adoption of standard boilerplate language to meet the requirements and recommend that a goal of high-quality reporting and disclosure be mandated so as ensure that meeting the criteria is not simply a formal process, but rather a well-considered, thoughtful and active approach.

ii) CFA UK believe that the proposed costs may be challenging given the current state of services needed to meet TCFD requirements.

iii) We believe TCFD reports should disclose the source of their data whether internal, from an asset manager or specialist providers as this will facilitate comparative analysis and lead to higher standards through increased transparency and greater peer learnings.

iv) We would highlight the importance of high-quality inputs into the process and expect that trustees appreciate both the needs and costs associated in executing their responsibilities with respect to climate change assessment.

v) We believe that scheme disclosures should share in detail which assets are covered by the TCFD analysis as well as detail specifically which assets are not covered, and the reasons why, as this will lead to higher quality standards through increased transparency and greater peer learnings in due course.

We believe quarterly reporting of emission and non-emission based data is excessive as quarterly reporting may not be prevalent for assets held within schemes and may place an additional administrative challenge with limited practical value.

- Given that the implementation of TCFD will be a new journey for many trustees and schemes, we believe that "peer learnings and standards" will play a crucial part in moving towards the goal of high-quality TCFD reporting. We also believe that given TCFD reporting can encompass different methodologies to deliver key data metrics, that it is in the best collective interest of schemes to share these methodologies and data inputs used in delivering the final metrics as far as is practically possible. This will also ultimately lead to higher-quality reporting across schemes as peers will learn and grow their knowledge of this new requirement by learning from one another along this journey towards optimal implementation of TCFD reporting.

- While we believe that quarterly reporting may be feasible for internal purposes given the frequency of data availability, we believe that annual reporting would be appropriate for regulatory reporting purposes, given the additional administrative challenges with prompt and accurate regulatory reporting. We would encourage the use of more frequent internal reporting e.g. quarterly or semi-annual so as to provide pension fund trustees relevant information when deciding on investment strategies.

- We are also cognizant of the risks of schemes and their service providers simply adopting standard boilerplate language when meeting TCFD requirements and would look towards the proposals to guide the expectation of trustees and schemes in usefully employing the information obtained from TCFD disclosures within their activities.

***Q5:* 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?**

While CFA UK agrees with the proposals, we would make the following comments:

i) We would caution against the adoption of standard boilerplate language to meet the requirements and recommend that a goal of high-quality analysis, reporting and disclosure be mandated so as ensure a well-considered, thoughtful and active approach.

ii) Given variations in the strategic direction of schemes and their respective asset liability profiles, we would recommend the adoption of short, medium and long term scenarios based on the unique situation of the scheme, the rationale for which has been clearly articulated and disclosed by the scheme. As such, schemes would should have the flexibility to effectively work within their clearly defined and well-rationalised respective time horizons.

Different schemes will have very unique circumstances and as such, each merits its own distinct view on time horizons applicable to its situation. An example may be of defined benefit schemes, many of which are now closed to new participants. As such, they may be dominated by retirees, with trustees possibly placing greater emphasis on shorter-term risks, given the underlying demographic of their plan participants. In contrast, another scheme with a far younger demographic may warrant greater risk weighting towards mid and longer time horizons, depending on their future obligations.

We also acknowledge that market dynamics may change with DB schemes opting to engage in transactions with insurance companies with respect to their obligations, again necessitating a different time horizon definition.

In addition we note that trustees of defined benefit schemes will need to identify and consider the impact of climate change risks on their sponsoring company. The outputs of this process should inform the funding and investment startegy of the pension scheme.

As such, it is challenging to employ a standard definition across schemes; however, we would advocate that schemes derive, rationalise and document clear time horizon definitions which they will be using for TCFD when describing the impact to their investment and funding strategy.

***Q6*: 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?

While CFA UK agrees with the proposals (6), we would make the following comments:

- We believe that that the language around the core 2°C or lower scenario should be modified to include changes to the core scenario as they may occur in the time following adoption of the proposals.
- We are cognizant that preparing accurate scenario analyses may be challenging given the current state of services and methodologies available.
- We raise concerns about consistency in methodology across schemes and service providers.
- We believe that an extreme climate scenario should be included in the scenario analysis alongside the core 2°C or lower scenario for comparison purposes.
- We believe qualitative scenario analysis has limited value and should only be allowed for first year of reporting if at all.
- We are troubled by the DWP's ambition for schemes to model liabilities (as well as assets) in the two proposed scenarios. Whilst an assumption could be made that interest rates (and therefore the discount rate for liabilities) will be lower in the worst case carbon scenario, thus leading to higher liabilities, this assumption cannot be relied on with a high degree of certainty. Furthermore, there are a number of other factors to consider besides interest rates (mortality rates, for example) and the prognosis on these in different climate scenarios is even more subject to guesswork at the present time[7]. In the absence of further guidance, CFA UK would suggest that the liabilities are initially not subject to different stresses in the two scenarios. This could be an area for further consultation.

CFA UK believe that proposing a specific 2°C or lower scenario at this point of time may run the risk of becoming outdated in the near term depending on the environmental impacts of the climate emergency. We recommend to use language guiding towards a "central scenario" which would have a longer remit, given that this scenario is open to change as needed. We appreciate that having a more general description of the central scenario may lead to alternative scenarios as part of TCFD, but would suggest that external guidance be taken when determining the central scenario, as well as other scenarios included in TCFD.

[7] Research highlights that in the UK there are more deaths due to cold winters than there are due to hot summers:
(https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/371103/Health_Effects_of_Climate_Change_in_the_UK_2012_V13_with_cover_accessible.pdf
https://www.actuaries.org.uk/system/files/field/document/Climate%20Change%20Mortality.pdf)

We have concerns about the ability of schemes, especially smaller schemes, to effectively implement TCFD climate scenarios due to the current state of services and methodologies and the fact that it will be challenging to outsource this to asset managers.

We also believe that schemes and trustees will need to play the role of aggregators in order to meet a scheme-wide TCFD view. Inputs into this process will come primarily from asset managers of commingled vehicles as well as Fiduciary Service Providers. These respective parties would most likely use different methodologies to derive their metrics, which would then be aggregated at the scheme level. This would raise concerns about the comparability of inputs across providers, as well as the accuracy of a final output at the scheme level.

As stated in our answer to question 5 above, we note that trustees of defined benefit pension schenes should also consider the impact of climate change risks on their sponsoring company.

Lastly, from a risk management perspective, we would also encourage the inclusion of an extreme climate scenario, so that trustees and schemes have properly incorporated possible "worst outcomes" within their investment decision-making and funding strategies.

***Q7:* 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?**

a) CFA UK agrees that trustees should adopt and maintain processes for identification, assessment and management of climate related risks as this puts in place a consistent framework. We would recommend, in an effort to avoid "boilerplate" language, that the guidance should emphasize scheme specific processes, as much as reasonably possible, to reflect the actuality of varied characteristics such as size, maturity, asset allocation, etc.
b) CFA UK agrees with the principle of integrating climate risks into the scheme's overall risk management as this would have the effect of directly addressing scheme risks. However, risk management is a complex area and we note the following:

    i. Integration of climate risk into the overall risk framework would necessitate changes to existing methodologies and access to robust time-series data (e.g. to calculate risk factor volatilities and correlations). This will take time to develop and rollout. We recommend setting an implementation deadline for this proposal;
    ii. Risk exposure and budgets drive a scheme investment strategy and in turn manager selection. This will in turn impose an extra duty on trustees to ensure their mandate guidelines and asset managers are capable of implementing and reporting on the risk objective;
    iii. There is significant emphasis on the role of asset managers in providing data for analysis and reporting. In reality asset managers' capabilities and appetite varies considerably. For example, specialist managers such as hedge funds,

private equity and property may not have the resources to source and collate scope 1, 2, and 3 emissions data on their investments. Another consideration is that risk management is a centralised process requiring data consistency, which is not guaranteed in a scheme that is reliant on several managers, and is mostly performed by an in-house investment team and investment consultants. There are a couple of implications to the above: firstly, schemes should be encouraged to use specialist climate risk measurement firms and investment consultants; and secondly, the cost of carrying out this exercise correctly at the outset is much greater that the costs suggested in the consultation.

c) CFA UK agrees with the disclosure requirement. As we state in our response to question 10, CFA UK recommends a standardised reporting format to ensure completeness, consistency and easy of comparative analysis.

***Q8:* 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?

a) CFA UK agrees that trustees should adopt and maintain processes for identification and reporting of GHG metrics. CFA UK would recommend that a specific measures, such as WACI or 2c scenario test, is mandated to allow for intra-scheme comparisons. The risk arising from the lack of a common metric is a confusing smorgasbord.

Schemes should be encouraged to report on more than two metrics so that trustees could also choose metrics, with suitable explanation, which they believe better suited to their circumstances. Trustees should provide a suitable explanation for their selection of metrics.

The metrics should evolve over time, so as to incorporate better availability of data, policy and regulatory changes as well as meaningful progress towards climate goals. In the medium term, we expect that we will see an increasing harmonisation of the approaches used.

CFA UK recommends that schemes should seek to maintain a strong element of consistency through time by maintaining original metrics in subsequent years, for a time at least, even if new 'improved' metrics are subsequently added to the reports as the industry develops best practice

b) CFA UK sees this as an aspirational goal, especially in the early years. Data quality, especially for scope 2 and 3, is grainy and potentially double counts. Enforcing this requirement now would prioritise data collection over robust and good process and methodology development. CFA UK recommends adoption of scope 2 and scope 3 as soon as robust and timely data is widely available.

c) CFA UK agrees with this proposal and also recommends the disclosure of the methodology used to compute the metric(s).

d) CFA UK agrees with the disclosure requirements. However, it is our strong preference for disclosures to cover all assets. In this regard, it would be valuable for schemes to receive guidance on calculating GHG intensity for generic assets such as cash, Gilt/ ILG, derivatives (Gilt Repo, interest rate swaps / inflation swaps) and bespoke assets such as property and insurance buy-in contracts. These asset classes currently account for a significant proportion of scheme assets (50%+, rising higher for mature schemes) and this is steadily increasing across the board. Potentially TPR or PCRIG could undertake this exercise.

***Q9:* 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?

a) CFA UK agrees with the premise of the proposal as an attempt to drive change. We foresee the outcome that meeting the target risks becoming the metric of success; thus distorting and distracting from the contextual focus of managing climate risk. As per our response to question 8, CFA UK recommends that trustees are prescribed a narrow choice of targets (e.g. WACI);

b) CFA UK agrees with calculating performance against target as a good principle. However, to minimise the risk of schemes gaming this target, we recommend that the target should be a range (i.e. tramlines) and that it should be set independently and that the target range is reviewed annually with a view to raising the bar over time. This should also encourage trustees to review regularly.

c) CFA UK believes that quarterly performance reporting would not be beneficial and indeed a potential impediment to the successful roll-out of TCFD reporting, given the frequency of the availability of fresh underlying data from corporates and asset managers. CFA UK recommends annual reporting to fit in with scheme's existing annual reporting cycles.

Q10: ***We propose that, for all schemes in scope. Do you agree with these proposals?***
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.

a) CFA UK agrees that trustees should be required to publish their TCFD report in full on a publicly available website where the report is accessible free of charge. Furthermore, trustees should be expected to site this report in a logical location [and in html format] to ensure that it can be easily found;
b) CFA UK would note that in its recent response to the FCA to its consultation CP20/3 on Corporate Climate Change Disclosure Reporting[8], CFA UK opined that corporates should include their TCFD report within their annual report ("R&A") and not incorporate it by a link. The principal reasoning behind that recommendation is CFA Institute's established advocacy position on the role of the R&A[9]. A company's R&A is commissioned for shareholders and since TCFD disclosures are material disclosures investors will want to see them in the R&A. Whilst other stakeholders are clearly interested in them, shareholders, as owners of the company should have them included in the R&A, commissioned by them on the basis of their materiality. By the same token, it would seem logical that scheme members should also demand the same rights in respect of the TCFD reporting of their pension fund. CFA UK notes also that non-incorporation runs the risk of the documents not being published on the same date and of 'window-dressing' in the Report & Accounts whereby the TCFD is incorporated by a link but positioned in slightly more glowing terms than might actually be the case in the actual report. CFA UK notes that many R&As are read in hard copy whereby links cannot be automatically followed through even when the reader has the time to do so;
c) CFA UK agrees with this proposal;

[8] Reference letter once sent
[9] Peters, Sandra J., Brydon Review response [letter to Sir Donald Brydon] (16 Aug. 2019) <https://www.cfainstitute.org/-/media/documents/comment-letter/2015-2019/20190816.ashx>

d) CFA UK agrees with this proposal. Furthermore, CFA UK recommends that additionally to their own publication format, schemes submit a standardised report to TPR and that this be made available publicly on TPR web-site portal. TPR could then conduct an annual aggregation exercise against which individual reports could also be compared.
e) CFA UK agrees with this proposal.

Q11: ***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?

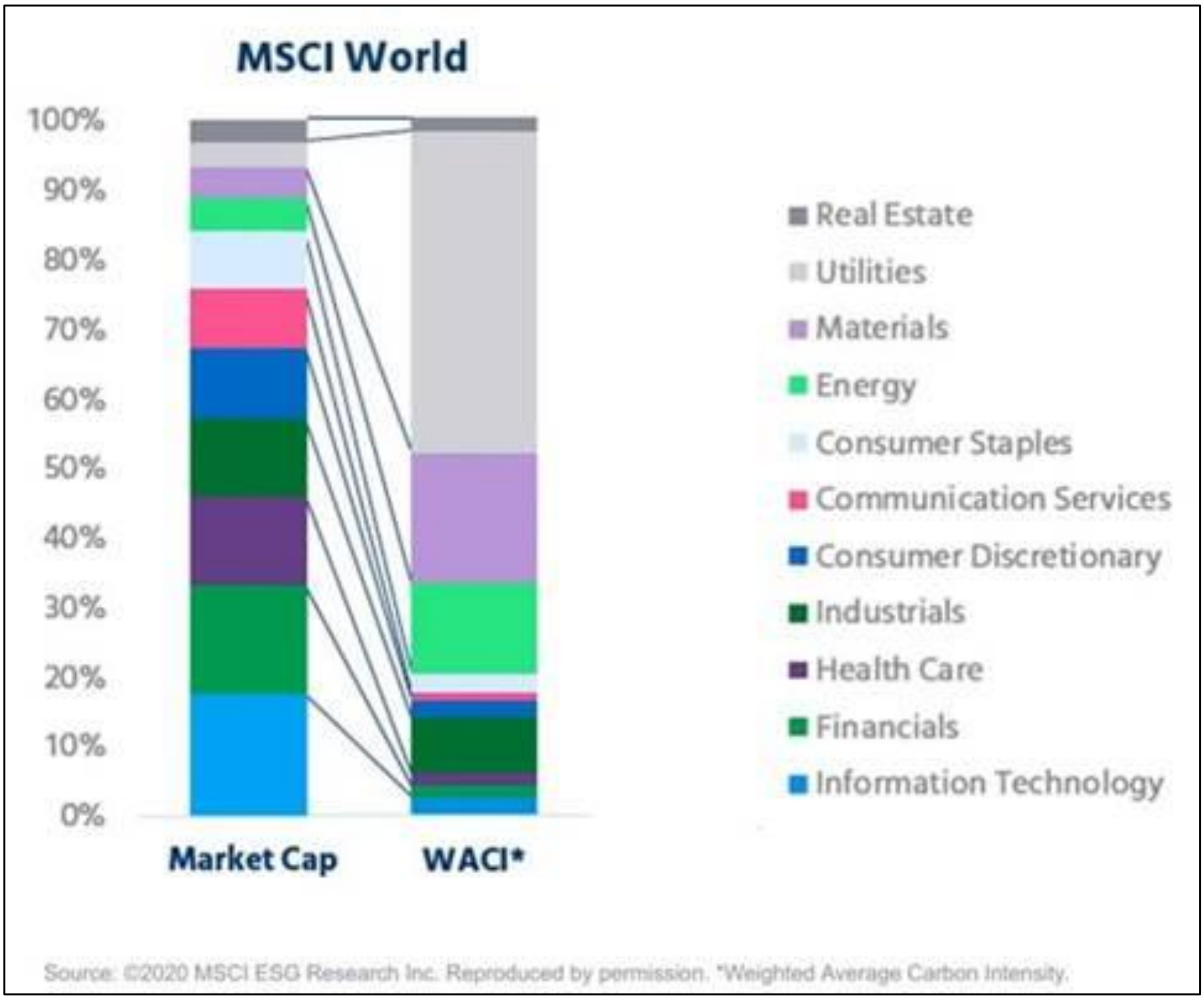
a) CFA UK agrees with the proposal that TPR should have the power to administer discretionary penalties. However, "inadequate" is open to interpretation and the best way to surmount this is for TPR to create a standardised reporting template which would also serve other useful functions as discussed earlier.
b) CFA UK agrees with the proposal that penalties are only mandatory in the event of total non-compliance. CFA UK proposes that TPR should disclose the identity of schemes in non-compliance or those whose disclosures are inadequate or filed after the deadline. This is the most powerful incentive to conform.
c) CFA UK agrees with the proposal and recommends increasing penalties for ongoing non-compliance.
d) CFA UK agrees with the proposal

Q12: ***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?***

- CFA UK recognises the importance of mitigating risks to pension scheme members arising from climate disruptions while also allowing scheme members to benefit from investment opportunities arising from decarbonisation.
- The anticipated wider societal impacts described in paragraph 95 of the impact assessment are consistent with the mission and values of CFA UK.

- While it may be possible for some schemes to meet the reporting requirements and the costs suggested in the impact assessment, CFA UK believes that for many schemes, and in particular those with less liquid portfolios, or portfolios that deviate further from market benchmarks, these cost estimates are overly optimistic.
- While CFA UK is broadly supportive of the aims of the proposals, the post implementation review process should be proactive and alert against adverse unforeseen consequences. Possible unforeseen consequences include:
  - Scheme trustees and beneficiaries fail to engage with the additional information, or engage with it in a different way to that intended with unfavourable consequences.
  - Investee firms that are resistant to complying with social norms, or firms that find the desired investor engagement disruptive to their businesses plans may seek private capital, or capital from other sources that enable them to bypass disclosure requirements and thus continue business as usual. Thus transparency among the 'worst offenders' might actually be reduced allowing them to outcompete firms accessible to UK pension schemes that have to comply with higher standards.
  - Climate change, and climate change risk also presents investment opportunities. One way by which schemes might seek to mitigate such risk is by increasing portfolio weights to investment themes that profit from climate disruption. If the overarching goal is to reduce man-made climate change, does investing in companies that will most likely profit from climate disruption conflict with that overarching goal?
  - In seeking to demonstrate best practice by showcasing low carbon intensity portfolios, it is possible that fund managers and scheme trustees, unwittingly or ortherwise, engage in herding behaviour. Such herding behaviour may cause distortions in the price of certain sectors or assets with the result that portfolio return volatility increases. For example, if the universe of quality assets exhibiting the required low-carbon characteristics is smaller than the value of funds wishing to invest in them, there may be a surfeit of low quality security issuance to meet the excess demand. A resulting worst case scenario is that large amounts of money are invested in projects that both fail to deliver decarbonisation, because the technology is not yet available, or not able to scale fast enough, and/or also destroy a large amount of retirement savings by delivering poor returns.
  - We note that under current (inadequate!) corporate reporting almost 50% of emissions come from utilities[10] (see chart below), with the balance predominantly from materials, energy and industrials. We further note that much of the long-end of the UK credit market, an important asset class for pensions schemes matching liabilities, is made up of utility bond issuance. If pension schemes act to improve their emissions score too fast, there must be a risk that the speed of implementation would not give certain industries time to adapt and further destroy pension scheme capital. If emission reduction targets were introduced once we were closer to implementation of scope 2 and 3 emissions, then this risk could be less material as carbon emissions would then show up as being more balanced between sectors.

[10] Source: MSCI ESG Research



Complying with the proposals may generate opportunity costs potentially distracting trustees' attention from other aspects of their fiduciary duty that may be just as, if not more, important to scheme beneficiaries.

Q13: ***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?

- CFA UK has no additional comments.