EMBRACING TCFD: PRACTICAL STEPS TO ADOPTING AND BENEFITING FROM THE TCFD FRAMEWORK

OCTOBER 2022
ABOUT A4S

- **Founded:** By His Majesty The King when he was The Prince of Wales, in 2004
- **Purpose:** Transform finance to deliver a sustainable future
- **Who we work with:** Engage at the most senior level across the end-to-end finance system

- **What we do:**
  - Inspire finance leaders to adopt sustainable and resilient business models
  - Transform financial decision making to enable an integrated approach, reflective of the opportunities and risks posed by environmental and social issues
  - Scale up action across the global finance and accounting community
OUR WORK WITH PENSION TRUSTEES

• Asset Owners Network

• Shaping what good looks like:
  • ESG Toolkit for Pension Chairs and Trustees
  • Webinars and roundtable sessions
  • Support collective voice on topics including TCFD, Net Zero, ISSB sustainability disclosure draft

• Collaborate with pension bodies and associations
WHAT IS THE TASKFORCE ON CLIMATE-RELATED FINANCIAL DISCLOSURES (TCFD) AND HOW DOES IT AFFECT PENSION SCHEMES IN THE UK?

• The TCFD was set up in 2015 by the Financial Stability Board and released its initial recommendations in 2017 for more effective climate-related disclosures.

• Looks at how climate change will affect the organization (not the other way round) ie for organizations to identify and disclose the risks and opportunities to the organizations due to climate change.

• Following the Occupational Pension Schemes Act 2021:
  • From 1st October 2021, occupational pension schemes with assets under management (AUM) of more than £5 billion must have produced and published (within seven months of the end of the scheme year underway on 1st October 2021) the scheme’s first annual TCFD report.
  • From October 2022, occupational pension schemes with AUM of more than £1 billion are captured on the same basis.

<table>
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<tr>
<th>Date</th>
<th>AUM Threshold</th>
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<tr>
<td>1st October 2021</td>
<td>&gt; £5 billion AUM</td>
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<tr>
<td>1st October 2022</td>
<td>&gt; £1 billion AUM</td>
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<td>&lt; £1 billion AUM</td>
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**AND WHY IS THIS IMPORTANT?**

- **Fiduciary duty** to provide long-term, risk-adjusted returns to our members is threatened by the impact of climate change both now and in the future.

- **Opportunities** as the global economy transitions to net zero and adapts to climate change, capital can be directed to new technologies, business models and asset classes.

- **Transition risk** from the realignment of the economic system towards low-carbon, climate-resilient or carbon positive solutions (eg via regulations or market forces).

- **Physical risk** as a result of extreme weather (eg damage to buildings and infrastructure) which can halt supply chains and/or close operations in vulnerable locations.

- **Litigation risk** (eg compliance with pension regulations; potential litigation faced by investee companies failing to mitigate, adapt or disclose; and potential litigation against pensions themselves).
WHAT ARE THE TCFD RECOMMENDATIONS FOR PENSION SCHEMES IN SCOPE?

- **Governance** – establish, maintain and disclose the trustees’ governance procedures around climate-related risks and opportunities.

- **Strategy** – disclose the actual and potential impacts of climate-related risks and opportunities on the pension scheme where that information is material.

- **Risk Management** – disclose how the trustees identify, assess, and manage climate-related risks.

- **Metrics and targets** – disclose the metrics and targets the trustees use to assess and manage climate-related risks and opportunities where that information is material.

- **Scenario analysis** – used to help trustees assess and manage the financially material risks that climate change may pose to their scheme.

- **Relevant knowledge requirements** – trustees must have an understanding of the principles relating to the identification, assessment and management of climate-related risks and opportunities to the scheme.
HOW CAN THE TCFD RECOMMENDATIONS HELP SMALLER SCHEMES?

- **Meet broader legal duties to manage climate-related risks** – TFCD provides a useful framework to work out governance needs and strategy development.

- **Assess the relevance of climate change (even for DB schemes winding up)** – climate related risks could affect the value of assets eg corporate debt and annuity pricing. TCFD helps trustees see their vulnerability in the short, medium and long term.

- Using climate scenario analysis can help you **assess your scheme’s resilience to different future outcomes** and how your assets or liabilities may be affected by different outcomes.

- **Strengthen an integrated risk management approach with scenario analysis** – using scenario analysis to look at potential climate impacts on investment, covenant and funding, will help you to understand how climate change will affect the employer’s ability to meet future contribution requirements.

- The risk framework as set out in the TCFD recommendations and PCRIG demonstrates the importance of have a **climate-related risks management process**. All trustees should revisit their risk registers and add climate-related risks as a consideration – risks to both the scheme’s investments and (for DB) funding and sponsor covenant.

- **Streamline!** – the TCFD framework is a global and cross industry accepted framework. By including the need to disclose in line with TCFD as part of fund manager selection criteria, it will ensure a certain amount of consistency of reporting across all 3rd party managers (therefore no need to translate disparate data into one format).

- **Communicate with members** - making your members aware about how you are considering climate-related risks and opportunities and how they are being managed will help build trust and public confidence with your members. Many pension schemes have conducted member surveys to see how important these issues are – they showing up as of high interest/concern.
TOP TIPS FOR SMALLER SCHEMES

• Use the TCFD framework to enhance overall governance processes and approaches

• Leverage peer networks and initiatives, like A4S, to share and learn from peers

• Don’t overcomplicate it and set measurable goals

• Get the whole Board involved and bought-in – start with the ESG Maturity Map for Pension Trustees

• Talk to your sponsor – many will have already adopted TCFD

• Talk to your service providers about following the TCFD framework
TAKE ADVANTAGE OF FREE RESOURCES AVAILABLE

- PCRIG is detailed and lists free scenario analysis tools to use
- The Pension Regulator’s guidance on governance and reporting of climate-related risks and opportunities
- Transition Pathway Initiative
- A4S’s ESG Toolkit for Pension Chairs and Trustees - Succinct and short guidance and pension case studies on:
  - TCFD elements eg scenario analysis, identifying metrics etc
  - Wider issues eg getting the most out of your service providers, embedding a net zero strategy, embedding sustainability into the employer covenant process
TOP TIPS FOR PENSION SCHEMES – GETTING STARTED

• Understand where you are at and get key decision makers on the same page > A4S’s ESG Maturity Map

• Leverage your peer networks and join existing collaborations, such as:
  • A4S’s Asset Owners Network (Pension scheme chairs)
  • Occupational Pensions Stewardship Council
  • UN-convened Net Zero Asset Owners Alliance
  • Principles for Responsible Investment
  • Transitions Pathway Initiative

• Use established processes, eg:
  • TCFD framework and scenario modelling – help understand your exposure to climate risk and identify your net zero targets and metrics
  • IIGCC’s Net Zero Investment Framework – test out different asset class approaches
  • Established internal processes eg investment beliefs / mandates – embed identified objectives and milestones
LEVERAGE YOUR POSITION TO EMBED ESG FACTORS INTO THE INVESTMENT PROCESS (ABOVE AND BEYOND REGULATORY REQUIREMENTS)*

• Set criteria to the manager procurement process, eg this could include:
  • Demonstrating their own TCFD implementation
  • Having a net zero transition plan
  • Being a signatory of UK Stewardship Code / net zero alliance etc

• Investment mandates – long-termism and long-term metrics

• Embrace the power of stewardship. Find out more:
  • Occupational Pensions Stewardship Council
  • Findings from the Taskforce on Pension Scheme Voting Implementation
  • A4S case studies on stewardship – eg Alecta, Church of England Pensions Board
  • Get active! (Shareholder resolution; respond to consultations; participate in collective initiatives)

*For further ‘Top Tips’ go to A4S website
ESG TOOLKIT FOR PENSION CHAIRS AND TRUSTEES
AN OVERVIEW
WHAT AND WHY

• A toolkit of resources that bring to life what good looks like.

• Aims to inspire action on next steps to mature the scheme’s ESG integration approach.

• A ‘live’ document with new resources continually being added.

• Supports trustees in discussions with fellow trustees, consultants and fund managers about practical actions they should take.

• Transferable to different jurisdictions and sizes (where appropriate).

• Also useful for service providers, actuaries and pension managers.

Access the toolkit here
KEY COMPONENTS

1. **An ESG maturity map** with suggested steps that schemes can take to progress on their ESG integration journey.

2. **Practical examples** of pension schemes to bring ‘what good looks like’ to life.

3. **Guidance material** to highlight the practical steps eg embedding ESG factors into different asset class portfolios.

Access the toolkit here
1. ESG MATURITY MAP

• Outlines ‘what good looks like’ and embeds ESG considerations into investment decisions, reporting, and engagement across the investment chain.

• Assesses what the scheme is currently doing and what steps can be taken to progress across 4 levels of maturity.

• For example:
  • Level 1: a Board could confidently speak about the role of asset owners in driving better corporate behaviour around ESG integration.
  • Level 3: a Board member would be expected to attend at least one investee company AGM per year, asking ESG-related questions as part of the engagement process.

Access the ESG Maturity Map here
1. ESG MATURITY MAP: LEVEL 0

**Level 0 – compliance only.**

This table sets out the minimum requirements that a UK pension scheme must currently comply with or needs to start processes in order to comply with near-term regulations as set out in the UK Pension Schemes Act 2021.

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<tr>
<th>Requirement – The Board must:</th>
<th>Deadline</th>
<th>Type of scheme</th>
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<tbody>
<tr>
<td>Include ESG and stewardship policies in its Statement of Investment Principles (SIP) and publish online.</td>
<td>By 1st October 2020 (if not earlier)</td>
<td>DB and DC / Hybrid</td>
</tr>
<tr>
<td>Publish an Implementation Statement explaining how it has implemented its SIP policies, including in ESG and stewardship, as well as provide further information on its asset manager and investment engagements.</td>
<td>First annual report from 1st October 2020 and no later than 1st October 2021</td>
<td>DC / Hybrid</td>
</tr>
<tr>
<td>Include a description of the voting behaviour by or on behalf of the Trustees including the use of proxies within the published Implementation Statement.</td>
<td>By 1st October 2021</td>
<td>DC / Hybrid</td>
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<tr>
<td>Publish an Implementation Statement explaining how it has implemented its SIP policies, including policies around voting and stewardship.</td>
<td>First annual report from 1st October 2020 and no later than 1st October 2021</td>
<td>DB</td>
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Following the coming into force of the Occupational Pension Schemes (Climate Change Governance and Reporting) Regulations 2021 on 1 October 2021, the Board in scope must:

- Disclose – within its governance policies – how it maintains oversight of climate-related risks and opportunities which are relevant to the scheme, as well as the role of any person who undertakes governance activities, or who advises or assists the Board with respect to governance (including legal advisers), in identifying, assessing and managing climate-related risks and opportunities – and the process by which the Board satisfies itself that the person is undertaking such identification, assessment and management.
- Identify and then assess the impact of climate-related risks and opportunities which it considers will have an effect over the short term, medium term and long term on the scheme’s investment strategy and, where relevant, the funding strategy.
- Undertake – as far as it is able – scenario analysis using at least two scenarios where there is an increase in the global average temperature, one of which is with an average temperature rise of between 1.5°C and 2°C above pre-industrial levels and then disclose the results.
- Disclose in a publicly available report, effective processes to identify, assess and manage climate-related risks, and ensure that this is integrated into the Board’s overall risk management of the scheme.
- Select, use and disclose at least two emissions-based metrics and one additional climate-related metric to calculate in relation to the scheme’s assets.
- Set a target for the scheme in relation to at least one of its chosen metrics and report annually on progress against the target.
- Have knowledge and understanding of the principles relating to the identification, assessment and management of risks and opportunities to its scheme arising from the effects of climate change, and implement trustee training where needed.

From 1st October 2021, with the scheme’s first annual TCFD report produced and published within seven months of the end of the scheme year under review on 1st October 2021 - Occupational pension schemes with assets under management (AUM) of more than £5 billion, authorised master trusts and collective money purchase schemes.

From October 2022, on the same basis – Occupational pension schemes with AUM of more than £1 billion.

**Access the ESG Maturity Map here**
1. ESG MATURITY MAP: IN PRACTICE

- A4S has written an accompanying guide to help trustees ‘workshop’ the maturity map with their Board.

Key features of the workshop guide:

- A step-by-step activity format and tips for maximizing engagement in a virtual context.
- An outputs template to record consensus on level of maturity per area, challenges identified and agreed next steps.
- Resource links table to signpost you to peer-case studies and guidance material.
- A commitments table to commit to progress with milestones and definitions of success.

Access the Workshop Guide here
2. PRACTICAL EXAMPLES

- A growing bank of case studies produced in collaboration with a variety of pension schemes (DB, DC, small, large, public, private, single/multi-employer).

- ‘In the voice’ of pensions schemes, focusing on practical steps for trustees, and including top tips for taking similar action.

Access the bank of practical examples here
TOPICS COVERED

- Engaging with service providers
- Stewardship
- TCFD reporting (including a deep dive into metric and target setting and scenario analysis)
- Setting Net Zero investment strategies
- Establishing opportunity funds
- Engaging with beneficiaries

Access the bank of practical examples [here](#)
3. GUIDANCE MATERIAL

- A growing bank of resources for chairs and trustees to integrate ESG into their decision-making and processes.
- Aim to facilitate discussions in-house and across the investment chain, highlighting key actions and steps that can be taken.

### Practical actions that trustees can take

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<tr>
<th>Area</th>
<th>Action</th>
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<tr>
<td>Education</td>
<td>- Arrange a forum to colloquise about the ESG risks and opportunities associated with measuring investment outcomes. This can include discussions on best practices and case studies. Each meeting should be structured to ensure that there is a clear agenda and objectives. The forum can be facilitated by an external expert or by the chair of the board. The discussions should be recorded and minutes should be circulated to all attendees. These can later be used to inform future decision-making.</td>
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<tr>
<td>Direct mail</td>
<td>- Ensure that the email addresses used are up to date and that the messages are relevant to the audience. This can be achieved by segmenting the list into different categories (e.g., stakeholders, investors, partners). The messages should be personalized and include a clear call-to-action. The success of the campaign can be measured by tracking open rates, click-through rates, and conversion rates.</td>
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<td>Engagement</td>
<td>- Establish a working group that includes representatives from different stakeholders to consult on ESG issues. The group should meet regularly to discuss the latest developments and share best practices. The working group can also help identify key performance indicators (KPIs) to monitor the progress of the initiatives.</td>
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<td>Collaboration</td>
<td>- Collaborate with other organizations, such as asset managers, to share resources and best practices. This can help streamline efforts and reduce duplication of effort. The collaboration can be formalized through joint initiatives, such as joint research projects or joint industry standards.</td>
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<td>Measurement</td>
<td>- Use performance metrics to evaluate the effectiveness of the ESG strategies. This can include metrics such as the reduction in carbon emissions, the increase in diversity and inclusion, and the decrease in the number of regulatory violations. The metrics should be regularly reviewed and adjusted as necessary.</td>
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**Access the guidance material here**
FEEDBACK

“We used the A4S Maturity Map in a Climate Training session with our Board. It was extremely useful to give the Trustees a picture of where we were, vis-a-vis other schemes, and where we might aspire to be across different parameters. It provided a good framework to prompt a thought-provoking discussion around our status, our goals and our specific areas of focus when it comes to climate risk.”
Catherine Claydon, Chair of BBC Pension Scheme and British Steel

“A4S’s ESG Toolkit for Pension Chairs and Trustees will help you navigate through a changing landscape.”
Emma Howard-Boyd, Chair of the Environment Agency and Co Chair of A4S’s Asset Owner Network

“A4S’s ESG Maturity Map helps put the trustees back in control of the agenda. It enabled me and my peer trustees to challenge and probe further into previous statements and responses from our investment consultants.”
Marcus Hurd, Professional Trustee, ndapt