ESG MATURITY MAP: EXAMPLE BEHAVIOURS FOR PENSION TRUSTEES

Embedding ESG considerations into pension schemes’ investment decisions, reporting and engagement across the investment chain

On the journey to embedding environmental, social and governance (ESG) considerations into a pension scheme strategy and processes, where do you think your scheme is along that journey? What actions could you take to deepen your approach further?

The levels outlined below are incremental, i.e. you cannot achieve Level 4 without completing previous levels in full. A Level 0 – Compliance only can be found at the end of this document, which outlines the minimum requirements that a Board of a UK pension scheme in scope must comply with.

Level 1 – Understanding

The Board has made several general remarks about the need to consider ESG factors when making investment decisions but has not undertaken any formal ESG action.

The Board
• has been made aware of the ESG factors that a pension scheme should consider when making investment decisions
• is aware of the impact that climate-related risks and opportunities might have on the scheme

Level 2 – Adopting

The Board has started to take action on planning and experimenting with a small approach to ESG providing an early stage commitment to the adoption of ESG considerations.

The Board
• has familiarity with the structure of this ESG assessment
• has asked what ESG factors the pension scheme should consider when making investment decisions

Level 3 – Deepening

The Board is in the process of embedding ESG factors into investment decisions and policies.

The Board
• has taken the view that ESG factors are a key consideration in the overall investment process
• has integrated ESG considerations into the investment decision-making process

Level 4 – Leading

The Board recognises that ESG is a key part of the scheme’s overall strategy.

The Board
• recognises that ESG factors are a key consideration in the overall investment process
• recognises that ESG factors need to be integrated into the investment decision-making process

A “best practice” guide is a good place to start for your scheme.

Alleviating risks to deliver sustainable outcomes

Historically defined contributions (PDI) pension schemes and default positions

The Board
• has a clear understanding of how PDI schemes function
• has an understanding of the nature and mechanics of PDI schemes

Making defined contributions (DC) schemes and adopting默认 contributions

The Board
• is a defined contribution scheme
• has defined contribution schemes

Making (eg frameworks and investment processes) decisions

The Board
• recognises that members may hold different views on ESG issues
• has considered what ESG issues and factors to consider

Proprietary of suite of funds

The Board
• has a suite of funds
• has a set of funds

Performing stewardship activities – improving another social or economic outcome

The Board
• has begun a procurement exercise to implement a sustainable default fund

Engagement along the investment chain

Engaging with scheme beneficiaries

The Board
• recognises the importance of engaging beneficiaries
• has considered the importance of member engagement

Engaging with scheme providers

The Board
• recognises the importance of engaging with providers
• has considered the importance of provider engagement

Engaging with investment consultants

The Board
• recognises the importance of engaging with consultants
• has considered the importance of consultant engagement

Engaging with investment managers

The Board
• recognises the importance of engaging with managers
• has considered the importance of manager engagement

Engaging with third parties

The Board
• recognises the importance of engaging with third parties
• has considered the importance of third party engagement

Reporting and collective action

The UK occupational schemes with under £1 billion AUM (UK local authority pension schemes, and non-UK schemes where TEPs implementation is not a current regulatory requirement)

The Board
• has considered how to improve its ESG performance
• has developed an effective ESG strategy

For UK occupational schemes with assets equal or exceeding £1 billion

The Board
• has considered how to improve its ESG performance
• has developed an effective ESG strategy

Please see Level 2 – Adopting for an outline of what is required to be required of the Board.
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.

<table>
<thead>
<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 this online.</td>
<td>By 1st October 2020 (if not earlier)</td>
<td>DB and DC / Hybrid</td>
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<tr>
<td>Publish ‘implementation statements’ 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>
</tr>
<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>
</tr>
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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 (excluding 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.

Possible developments after the Pension Schemes Act 2021

- In the future, the Board may need to oversee the publication of the contribution of schemes’ assets to climate change (the “implied temperature rise” of the scheme).

- In the future, the Board may also need to disclose what percentage of its pension scheme activities are “green”, in line with a UK taxonomy.