West Midlands Pension Fund

10th March 2021

David Farrar, Climate Change and Responsible Investment Team
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Dear David,

West Midlands Pension Fund Response: Taking action on climate risk: improving governance and reporting by occupational pension schemes – response and consultation on regulations

We are grateful for the opportunity to respond to this consultation.

The West Midlands Pension Fund is part of the Local Government Pension Scheme (LGPS) and is one of the largest schemes in the country and as such takes it responsibilities in respect of climate change very seriously. Indeed, the Fund was recognised as one of those 'more engaged' when the Environmental Audit Committee reviewed the policies of the 25 largest pension schemes in the UK in 2018.

Whilst we do not believe that the current provisions of this consultation are aimed at the LGPS and the Fund is excluded from the scope of mandatory climate governance and TCFD reporting, operating as it does under the LGPS regulations, we believe it appropriate to respond on policy matters relating to climate change. The Fund has always looked to adopt best practice in respect of its Responsible Investment activity and takes an evidence-based approach to climate change for a number of years issuing its four-year Climate Risk Management Framework and Strategy in 2019. The Fund has undertaken reporting in line with TCFD recommendations since 2017 and is strongly supportive of transparency in all reporting across the pension and asset management industry.

We also recognise that regulations on climate governance and reporting are likely to be captured at a future date within the LGPS regulations and therefore believe it appropriate to comment at an early stage on such critical policy developments.

We welcome the government's response to the August 2020 consultation, noting the areas of feedback from West Midlands Pension Fund and others taken on board and provide enclosed our comments in response to the further questions raised in the January 2021 consultation.

Rachel Brothwood
Director of Pensions

West Midlands Pension Fund

Response to consultation questions

Question 1: Scope and Timing		
a)	Do you have comments on the proposals to change the "reference date" used for the purposes of determining whether a scheme is in scope, or the arrangements made for schemes which obtain their audited accounts later than 1 October 2021, or 1 October 2022?	We are supportive of the timetable put forward for implementation.
b)	Do you have comments on the draft regulations on scope and timing? Please include in your answer any comments on whether you consider that they meet the policy intent stated in this chapter.	Climate change poses a risk to all schemes irrespective of size. We recognise that smaller schemes may find compliance more difficult than larger schemes with dedicated responsible investment resources, therefore we ask policy makers to proactively encourage and support smaller schemes to actively manage climate risk; the TCFD framework provides a practicable approach to do this which we would hope could become accessible to all schemes in time. We have concerns surrounding the seven month publication deadline from scheme year end. In the first instance, we consider seven months to be too short a time frame for publication, particularly during the early years of implementation where market capacity issues and Trustee knowledge and understanding need to be developed. We suggest that consideration is given to phasing in from a longer reporting period initially, for example 15 months, reducing to 12 months then reaching 7 months after four to five years. Noting the Trustees are expected to set and review progress against targets, this is a more realistic timeframe for publication of an action or response to the output; alongside the disclosure itself. We would encourage clarification of requirements to be set out in statutory guidance, in order to avoid significant variation in standards of measurement and reporting across individual schemes given differing levels of capacity, resources and expertise and to support a cost effective response to increasing regulatory and disclosure requirements.

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Question 2: Trustee Knowledge and Understanding		
a)	Do you have any comments on the draft regulations on trustee knowledge and understanding?	We support the need for trustees to be equipped with sufficient knowledge and expertise to be able to make informed decisions regarding the financial risks and opportunities arising as a result of climate change. Trustees should be encouraged to look beyond the raw analysis and ensure climate risks are considered within development of strategy and decision making; with appropriate caution applied to metrics based on estimates and incomplete data.
b)	Do you have any comments on the draft guidance? Please include in your answer any comments on whether you consider that they meet the policy intent stated in this chapter.	We note the potential spectrum of Trustee Knowledge and Understanding that may prevail in the early years of the regime and encourage the Pensions Regulator to clearly articulate what is expected of trustees. Given both the regulatory and practical need for schemes to engage advisors, we would also like to see the DWP take steps to work with the FCA to ensure that relevant levels of skills and climate knowledge are part of the authorisation regime for investment consultants and managers.
Question 3: Governance		
a)	Do you have any comments on the draft regulations on governance?	We support the proposal that Trustees should establish and maintain oversight of climate risks and opportunities on an ongoing basis, recognising that climate risks are one of a number of risks that trustees need to manage. However, we strongly acknowledge and agreed that holistic climate risk management is required to fully aligned with the fiduciary responsibilities of the Trustees.
b)	Do you have any comments on the draft statutory guidance? Please include in your answer any comments on whether you consider that they meet the policy intent stated in this chapter	As above.
Question 4: Strategy		
a)	Do you have any comments on the draft regulations on strategy?	We support the policy proposals for greater disclosure and transparency in climate reporting, although recognise the limitations of current reporting. We welcome the support proposed in terms of definitions and examples to be included in the statutory guidance.

b)	Do you have any comments on the draft statutory guidance? Please include in your answer any comments on whether you consider that they meet the policy intent stated in this chapter.	As above.
Question 5: Scenario Analysis		
a)	Do you have any comments on the provisions on scenario analysis in the draft regulations?	We are aware that some vendors have found it difficult to accurately model 1.5°C climate scenarios. We recognise the important of alignment with 1.5°C as set out in the Paris Agreement, and hope that its inclusion within regulations will help create the momentum needed for the continued development of scenario analysis. We agree that requirements should be expected to be applied only “in as far as they are able”, as the text denotes.
b)	Do you have any comments on the proposal that all assets of the scheme, including relevant contracts of insurance, are within scope for scenario analysis	We support the policy proposals and agree that all assets should be in scope for scenario analysis. We note that there are likely to be data gaps on the information available and indeed in assessing our own climate risk reporting, we have noted that there have been significant limitations on being able to report in a meaningful way on assets outside of listed equities and fixed income.
c)	Do you have any comments on the draft statutory guidance on scenario analysis? Please include in your answer any comments on whether you consider that they meet the policy intent stated in this chapter.	We acknowledge that some research/ data providers can be hesitant in allowing funds to publicly share climate scenario analysis and carbon footprinting results. We foresee that this could be an impediment to the request for full transparency and disclosure, particularly in relation to underlying methodology.

Chapter 6: Risk Management		
a)	Do you have any comments on the draft regulations on risk management?	We support the policy proposals, however, would avoid being overly prescriptive. Data capture and identification remains very much in the development phase and this is likely to lead to some limitations in reporting.
b)	Do you have any comments on the draft statutory guidance? Please include in your answer any comments on whether you consider that they meet the policy intent stated in this chapter.	As above.
Chapter 7: Metrics		
a)	Do you have any comments on the draft regulations on metrics?	We agree that trustees should be required to obtain metrics annually, rather than quarterly, and for the extension of the 'as far as able' provision to the calculation and use of data. We also welcome the acknowledgement that metrics need to be appropriate to the underlying asset class. We also agree that analysing scope 1,2 and 3 emissions separately avoids some of the issues associated with double counting. We have concerns at this point in time that analysis of scope 3 emissions would require reliance on estimated scope 3 data, such analysis may be of limited benefit. However, we hope that the Government's proposals will result in better disclosure from corporates and more sophisticated and accurate methods of estimation from vendors. Evolving metrics and methodologies makes year on year comparison of results more challenging.
b)	Do you have any comments on the draft statutory guidance? Please include in your answer any comments on whether you consider that they meet the policy intent stated in this chapter.	We welcome and acknowledge that these metrics are still developing for consideration of liability and covenant risk but would suggest and welcome clarity that consideration of funding risks should align with the timeframe for scenario analysis on the assets, to enable a proportionate and integrated risk management approach. We welcome the statement that these metrics are not to be used as triggers to invest or divest, but would ask that the guidance is clearer and goes further on this point to note that whilst they may be a factor which

		informs decision making, all investment and funding decision making should continue to be made in the context of the wider scheme-specific investment and funding strategy and the objectives set within these. We would separately welcome recognition that these could be volatile and change as strategies, data and analysis tools develop so a level of "re-basing" should be accepted and welcomed (where feasible) to ensure meaningful insight to risk management.
Chapter 8: Targets		
a)	Do you have any comments on the draft regulations on targets?	We previously stated that the proposal to measure quarterly is overly prescriptive at this stage given both the ability to capture data accurately but also the potential additional resourcing burdens that this places on schemes until such time as the ability to undertake measurement is more readily available, so welcome and support the revised expectations of annual target monitoring.
b)	Do you have any comments on the draft statutory guidance? Please include in your answer any comments on whether you consider that they meet the policy intent stated in this chapter.	We would welcome a more explicit statement to confirm these should be scheme-specific ; we would also like to see clear purpose for targets set to be clear that these are intended to inform risk management and are aligned with the strategy determined by the scheme. We believe that the guidance provides flexibility as to which metric to set the target against and allows for discretion as to which asset class to set it against. Whilst we welcome this flexibility, transparency around the purpose of each target and the risk management benefits it is looking to achieve, will aid the end reader.
Chapter 9: Disclosure		
a)	Do you have any comments on the draft regulations on disclosure?	We agree with the outline proposals to make climate change reporting transparent and accessible. We would support inclusion of a minimum high level TCFD report in a Scheme's annual report and accounts with links to wider report as available. Including a link in member annual benefit statements would also offer a solution to making the TCFD reporting to the scheme membership base. This would not prevent other mechanisms for reporting to members which can include more regular newsletters. Consideration of the different audiences will need some consideration, including context of the scheme and the choices available to the members.
b)	Do you have any comments on the draft statutory guidance?	As noted in answer 1b, we have concerns surrounding the seven month publication deadline from scheme year end. In the first instance, we consider seven months to be too short a time frame for publication, particularly during the early years of implementation where market capacity issues and Trustee knowledge

	Please include in your answer any comments on whether you consider that they meet the policy intent stated in this chapter.	and understanding needs to be developed. We suggest that consideration is given to phasing in from a longer reporting period initially, for example 15 months, reducing to 12 months then reaching 7 months after four to five years. Noting the Trustees are expected to set and review progress against targets, this is a more realistic timeframe for publication of an action or response to the output; alongside the disclosure itself.
Chapter 10: Penalties		
a)	Do you have any comments on the draft regulations on penalties? Please include in your answer any comments you have on whether you consider that they meet the policy intent stated in this chapter	Whilst we agree that there should be penalties for non-disclosure, we believe that there needs to be a reasonable timeframe to enable schemes to adapt to the new reporting requirements.
Chapter 11: Impacts		
	In relation to the policy changes we have made, do you have any comments on the regulatory burdens to business and benefits, and wider non-monetised impacts which are estimated and discussed in the draft impact assessment?	We consider that the costs of conducting meaningful scenario analysis and carbon foot printing analysis aimed at providing portfolio specific insights are significantly underestimated in the consultation. Analysis of costs incurred are estimates at this stage and the scope of requirements should be reviewed (at scheme and policy level) in accordance with future assessment of added value. Comprehensive datasets are required and in the case of scenario analysis assistance with interpreting and analysing the outputs is helpful and may be essential for smaller schemes.
Chapter 12: Any Other Comments		
	Do you have any other comments you would like to raise?	We welcome the principles (Section 95) as a point of focus for schemes assessing their response.