SQUIRE PATTON BOGGS

Pensions Quick Guide

Publication of TCFD Reports

Why Are Large Schemes Being Required to Undertake Additional Governance and Reporting Requirements?

The UK government has committed to bringing all greenhouse gas emissions to net zero by 2050. It has also announced its intention to make disclosures aligned with the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD) mandatory across the UK economy by 2025. Requiring pension schemes to publish TCFD reports is a step in that direction and the government is starting with the largest occupational pension schemes.

The Pension Schemes Act 2021 includes a provision enabling the government to issue regulations and statutory guidance that would require pension schemes to undertake mandatory governance and reporting in relation to the effects of climate-related risks. Following consultation, the government issued regulations and statutory guidance implementing those requirements for the largest occupational pension schemes.

Which Schemes Are in Scope and From What Date?

Type of Scheme	Measurement Date	Governance Requirements	Reporting and Disclosure Requirements
Occupational scheme with relevant assets of £5 billion or more	First scheme year end falling on or after 1 March 2020	From 1 October 2021 in relation to a scheme year that is underway or (unless it is an "earmarked" scheme) if later, the date on which the trustees obtain audited accounts in relation to that scheme year-end date	Within seven months of the end of the scheme year that is underway on 1 October 2021
Occupational scheme with relevant assets of £1 billion or more at scheme year date ending between 1 March 2021 and 28 February 2022	First scheme year end falling on or after 1 March 2021	From 1 October 2022 in relation to a scheme year that is underway or, (unless it is an "earmarked" scheme) if later, the date on which the trustees obtain audited accounts in relation to that scheme year-end date	Within seven months of the end of the scheme year that is underway on 1 October 2022
Occupational scheme with relevant assets of £1 billion or more at scheme year date ending on or after 1 March 2022	Any scheme year ending on or after 1 March 2022	The scheme year commencement date that is one scheme year and one day after that scheme year-end date (for example, for a scheme year ending 31 December 2022, the duties would apply from 1 January 2024)	Within seven months of the end of the scheme year in which the trustees commence the governance requirements
Authorised master trust	1 October 2021	Current scheme year from 1 October 2021 to end of that scheme year and subsequent years	Within seven months of the end of the scheme year underway on 1 October 2021
Authorised collective money purchase (CMP) scheme	1 October 2021	Current scheme year from 1 October 2021 to end of that scheme year and subsequent years	Within seven months of the end of the scheme year underway on 1 October 2021

Generally speaking, an "earmarked" scheme means an insured defined contribution scheme. Also, generally speaking, "relevant assets" means the net asset value of the scheme, but excluding the value of any contracts of insurance that have been bought to secure benefits.

The asset threshold applies at scheme level, rather than at section level.

Could a Scheme Fall Out of Scope?

An authorised master trust/authorised CMP scheme would fall out of scope if it ceases to be authorised and had less than £500 million in relevant assets on the scheme year-end date immediately preceding the scheme year in which authorisation ceased. All requirements would fall away immediately.

Any other scheme would fall out of scope if it ceases to have relevant assets of £500 million on any subsequent scheme year-end date. While the governance requirements would fall away from the scheme year-end date, the reporting and disclosure requirements must still be met within seven months of the end of that scheme year.

What Do the Regulations Do?

There are two sets of governance and reporting regulations, which came into force on 1 October 2021. There are seven key themes running through the regulations. A high-level overview is contained in the boxes.

Governance

Trustees must establish and maintain oversight of the climate-related risks and opportunities that are relevant to the scheme.

Trustees must establish and maintain suitable processes.

Strategy

Trustees must, on an ongoing basis, identify and assess the impact of climate-related risks and opportunities that they consider will have an effect over the short, medium and long term on the scheme's investment strategy and funding strategy.

Risk Management

Trustees must establish and maintain processes for the purpose of enabling them to identify, assess and manage climate-related risks that are relevant to the scheme.

Management of risks would need to be integrated into a scheme's overall integrated risk management.

Metrics and Targets

Each year, the trustees must obtain the "scope 1", "scope 2" and "scope 3" greenhouse gas emissions attributable to their scheme assets: i.e. (1) emissions directly attributable to scheme activities; (2) emissions indirectly attributable to electricity used by the scheme; and (3) other indirect emissions from activities of the scheme that occur from sources that the scheme does not directly control. They must also obtain data to calculate a portfolio alignment metric.

(Scope 3 is not required for first year).

Trustees must select at least four metrics, including one absolute emissions metric (total greenhouse gas emissions attributable to the scheme's assets) and one emissions intensity metric (total greenhouse gas emissions attributable to the scheme's assets per unit of currency) and one portfolio alignment metric, and use the data obtained to calculate these metrics.

Trustees must set a target for the scheme in relation to at least one of the metrics that they have selected to calculate.

Trustees must measure annually, as far as they are able, the performance of the scheme against any target they have set and decide whether to retain or replace it.

Trustee Knowledge and Understanding

Trustees must have the appropriate degree of knowledge and understanding of how to identify, assess and manage risks to occupational pension schemes arising from the effects of climate change and opportunities relating to climate change, to enable them to meet the requirements in Part 1 of the Schedule to the Climate Change Governance and Reporting Regulations.

Scenario Analysis

Trustees must, as far as they are able, undertake scenario analysis every three years with annual reviews. The analysis must consider potential impact and resilience in at least two scenarios where there is an increase in the global average temperature, including where the global average temperature increase must be within the range of 1.5 to 2 degrees Celsius above pre-industrial levels.

Reporting and Disclosure

Trustees must produce a TCFD report, the contents of which are specified in the regulations.

The report must be published on a website accessible free of charge.

The website address must be stated in the pension scheme return.

Information about the TCFD report must be included in the annual report, annual benefit statements and any annual funding statement.

What Does "As far as They Are Able" Actually Mean?

Trustees must carry out scenario analysis, obtain data, calculate and use metrics and measure performance against trustee-set targets "as far as they are able".

The regulations say this means taking "all such steps as are reasonable and proportionate in the particular circumstances taking into account… the costs, or likely costs, which will be incurred by the scheme… and… the time required to be spent by the trustees or people to whom the trustees have delegated responsibility".

The statutory guidance provides further information on the steps that trustees should take to meet requirements "as far as they are able".

Is There Any Guidance?

Trustees must have regard to statutory guidance. The statutory guidance (which came into force at the same time as the regulations) sets out how trustees should meet the requirements in the regulations and how they should report in line with the TCFD recommendations.

Where trustees choose to diverge from a "should" requirement in the statutory guidance, they must explain their reasons for doing so in their TCFD report.

The government has also published final form non-statutory guidance, prepared by the Pensions Climate Risk Group. This non-statutory guidance provides a good source of supplementary practical materials, which will help trustees to meet their statutory duties. The Pensions Regulator (TPR) has also published guidance, which trustees should take into account.

Some Practical Points

Do	Don't
Do ensure that the TCFD report is signed by the Chair (or interim Chair) of trustees (this is a legal requirement).	**Don't** forget the regulations allow the manuscript signature of the person who has signed the TCFD report to be omitted from the version published online.
Do arrange training for the trustee board so that they can meet the knowledge and understanding requirements of the regulations. The DWP has suggested that whether the TCFD report can be easily understood by members will be a good test of how well the trustees understand the issues.	**Don't** forget that a scheme does not automatically fall out of scope if it no longer meets the measurement threshold. Its asset value must fall below £500 million before the out of scope provisions apply.
Do remember your usual good governance processes and update the scheme's risk register, integrated risk management plan and prepare a breach response plan.	**Don't** forget the employer – update information sharing agreements so that you can consider the employer's approach to climate risk and ESG and take account of these when assessing the employer covenant.
Do take a proportionate approach. The government and TPR recognise that some of the requirements will pose a challenge because data and information might not be available.	**Don't** leave compliance until the end of the year – the strategy requirements need to be complied with on an "ongoing" basis and you need to ensure investment managers have appropriate processes and systems in place throughout the year.

What Are the Consequences of Failing to Comply?

A complete failure to publish a TCFD report will attract a mandatory penalty of at least £2,500, with other penalties subject to the discretion of TPR.

The maximum penalties for failing to comply with the regulations are £5,000 per individual and £50,000 per corporate.

TPR can also issue a compliance notice under the regulations and an improvement notice under the Pensions Act 2004 to anyone contravening provisions of that Act, such as the trustee knowledge and understanding requirements. If a person fails to comply with a compliance notice or an improvement notice, maximum penalties of £5,000 (individual) and £50,000 (corporate) will also apply.

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