

# Sixty second summary

## Aligning views on the LGPS climate change risk consultation

With the impact of climate change being felt more acutely across the globe, on 1 September, the UK Government launched their consultation on Governance and Reporting of climate risks. The proposals apply to LGPS funds in England and Wales with regulations expected to come into force by April 2023. In this short update, we note the key proposals set out in the consultation.

### Basic principles of the reporting framework

As widely expected, the [consultation](#) follows the Taskforce for Climate-related Financial Disclosures (TCFD) framework and will require Administering Authorities to consider and report against the four key areas of governance, strategy, risk management, and metrics and targets. The aim of this framework is to help the LGPS demonstrate how the consideration of climate change risks and opportunities are integrated into each Authority's entire decision-making process.

The proposals under the consultation are similar to the [new requirements](#) that came into force for private sector pension funds in October 2021 but include some key differences in order to reflect the needs of the LGPS, the desire to have consistency in data and reporting, and to try to positively impact the ability to accurately measure and report climate risk and emissions data.

### Key requirements proposed in the consultation

- Establish and maintain a **Governance** approach for oversight of climate risks and opportunities.
- Assess the impact of climate-related risks and opportunities on funding and investment **strategies**.
- Carry out **scenario analysis** reflecting different temperature pathway alignments (one being Paris aligned).
- Establish and maintain processes for identifying and managing climate-related **risks and opportunities**.
- Report on a minimum of four prescribed **climate metrics** which need to be measured and disclosed annually.
- Set a (non-binding) **target** in relation to one metric, chosen by the Authority.
- As part of ongoing **disclosure requirements** Authorities will need to publish an **annual climate risk report** with the Scheme Advisory Board also preparing an annual report, linking to individual reports and aggregate figures for the prescribed metrics.
- Other requirements including taking **proper advice** and having the **knowledge and skills** required.

The consultation opened on 1 September and has a closing date of 24 November 2022. The relevant regulations are expected to be in force by April 2023 with Authorities' first report due by December 2024 covering the 2023/24 scheme year.

### Spot the difference

The requirements set out in the consultation include some key differences to those applying to private sector schemes. The first is that there is no minimum size requirement with the proposals applying to all LGPS funds in England and Wales. Other notable differences are:

#### Metrics

The proposals are prescriptive in the metrics which LGPS funds will need to report against. Four metrics are proposed – Total Carbon Emissions, Carbon Footprint, Data Quality and a Paris Alignment Metric. For emissions metrics, while acknowledging the challenges of availability and reliability of data, the proposals are for metrics to cover Scope 1, 2 and 3 emissions to give the fullest possible picture of carbon exposure.

Data quality has been a common metric for pension funds to consider but the proposals list this as a prescribed metric, whereby funds will set out the percentage of data across their assets which is Verified, Reported, Estimated or Unavailable. We recently commented on the [challenges](#) of getting accurate data within private markets mandates and we hope these proposals will shine further light on data gaps, thereby helping drive positive improvements in reporting standards.

With regards to the Paris Alignment Metric, whilst the consultation supports models such as implied temperature rise (ITR) and expects many funds will choose to report these metrics, the proposed requirement will be for funds to report against a binary target, setting out the percentage of their total assets with declared net zero or Paris-aligned targets.

### **Mandating compliance**

As any fund that has already reported against TCFD will know, gathering data, carrying out climate analysis, documenting processes and preparing reports can take a significant amount of time and effort. The consultation notes the challenges of carrying out this work, proposing that Authorities are expected to follow the requirements “as far as they are able”. This means Authorities are able to act now to address climate-related risks and opportunities without waiting for perfect data.

### **Dual requirements for disclosures**

Climate risk reporting and analysis is an evolving area. It can sometimes be complex, requiring specialist knowledge or expertise, and therefore it's important that the LGPS' approach to managing these risks can be reported in a way that stands up to external scrutiny. The consultation sets out the dual requirements for reporting to be understood by lay readers as well as by those wishing to interrogate data and approaches in more detail. We hope this will help to demonstrate the positive work the LGPS has been doing and will continue to do to address climate-related risks and opportunities.

### **Statutory guidance**

DLUHC proposes to publish statutory guidance to support Authorities in the implementation of the proposals. The expectation is that this will draw on guidance already available to investors whilst seeking to establish consistency across the LGPS. It is also proposed that the Scheme Advisory Board creates a standard reporting template which funds will be required to follow in producing their Climate Risk Report. However, we note that this could create a risk that individual funds do not think specifically about their own circumstances.

### **Scheme wide reporting**

Linked to the above requirement, the proposals on Scheme wide reporting when combined with the consistency of metrics and data reporting will allow aggregate reporting on emissions, data quality and Paris Alignment. We expect this to be a useful tool in engaging with companies, managers, industry and government on these issues.

### **Alignment with Pools**

The consultation highlights the important role that LGPS pools play in addressing and managing climate risk. While Authorities work closely with their pools (and assets invested through pools continues to increase), agreeing objectives and targets on climate remains the responsibility of individual Authorities. The consultation, however, proposes that Authorities and pool strategies may benefit from alignment, either for consistency of analysis or bringing further benefits of scale.

## **Next steps**

The consultation on Governance and Reporting of climate change risks for the LGPS is one that has been expected for some time. The proposals highlight some of the challenges faced by all investors in addressing and managing these risks, but also the potential to drive positive change through engagement and improving the consistency and accuracy of reported data.

We will be preparing our own response to the consultation ahead of 24 November, which we will share in due course but all LGPS stakeholders should consider the proposals and whether to respond to the 12 consultation questions. If you wish to discuss the consultation further, please contact your Hymans consultant, or get in touch [here](#).