

# Sixty second summary



## Government response to consultation on 4th TCFD metric and Stewardship Guidance

The DWP published its response to the recent consultation on introduction of a portfolio alignment metric to TCFD governance and reporting requirements. The consultation response also finalised the statutory guidance on stewardship for pension schemes.

There were no significant surprises in the consultation [response](#). Pension schemes which are subject to TCFD will be obliged to include an appropriate forward-looking metric from 1 October 2022 when considering their approach to the management of climate-related risks. The [guidance](#) on stewardship takes immediate effect, although the statutory elements of this guidance, which apply only to Implementation Statements, also take effect for scheme years ending on or after 1 October 2022.

### An additional TCFD metric

The climate metrics that included within the TCFD governance and reporting requirements generally sought to measure backward looking climate considerations, such as carbon emissions. A portfolio alignment metric is intended to be forward looking in its approach, seeking to measure the extent to which companies or assets are aligned with the changes necessary to meet the Paris Agreement. There are three different types of portfolio alignment metrics that trustees can choose to measure:

- **Binary target measurements.** These seek to measure information such as the number of companies within a portfolio that have a net zero objective or plan, or the number of companies that have plans which have been accredited by the Science Based Targets initiative.
- **Benchmark divergence targets.** These seek to assess the performance of companies in a portfolio against an approach benchmark, based on projected climate scenarios.
- **Implied temperature-rise models.** These methods take the policies and strategies that companies in a portfolio have in place and, using projected climate scenarios, translate these into an expected outcome expressed in the form of a temperature rise.

Trustees will need to select one of these metrics to be included in their governance and reporting, seeking to use the same approach across the portfolio where possible. This requirement will apply to all schemes within the scope of TCFD from 1 October 2022. Trustees must measure portfolio alignment *as far as they are able*, recognising that data challenges may be a barrier to measurement in some asset classes.

*The introduction of a forward-looking metric is welcome and should help ensure that the discussion and actions taken to address climate change focus as much on the changes that organisations are taking to change as their current position. Binary target type metrics are likely to be the most common choice of metric in the short term given their simplicity and relative ease of taking action to influence. Trustees should ensure they are engaging with their investment consultant to incorporate as they prepare for TCFD over coming months.*

### Statutory guidance on stewardship and the Implementation Statement (IS)

The DWP has published guidance which seeks to clarify aspects of stewardship. The guidance is a mix of statutory and non-statutory guidance and applies to the preparation of Statements of Investment Principles and Implementation Statements. The statutory elements of the guidance refer only to Implementation Statements prepared for scheme years ending on or after 1 October 2022. However, the DWP has encouraged trustees to follow this and the other non-statutory elements of the guidance with immediate effect.

The Statutory elements of the guidance address in greater detail how trustees should approach both the implementation of their stewardship policies, and the preparation of their IS. The guidance also states that trustees are the owners of the IS and whilst advice can be obtained on its preparation, this is not a requirement. Key aspects of the statutory guidance related to stewardship are set out below. There is also additional guidance related to the extended IS requirements of DC and hybrid schemes.

### Implementation Statement

- The Pensions Regulator is the primary audience for the IS. It should be in plain English as far as possible, such that a reasonably engaged and informed member could interpret and understand the disclosures. Trustees may incorporate or duplicate sections from their stewardship report to the FRC in the IS, although the IS must be able to be read as a standalone document.
- In preparing the IS Trustees 'may wish to consider' the extent of alignment with Principle 6 of the UK Stewardship Code. This asks signatories to take account of client and beneficiary needs and communicate the activities and outcomes of their stewardship and investment to them.

### Voting behaviour and significant votes

- The IS must state how the policy covered in the SIP on the exercise of (voting and engagement) rights has been followed. Trustees should explain whether the voting undertaken on their behalf was reflective of the scheme's voting policy/stewardship activities. Where it has not been, the trustees should explain in the IS why that was the case.
- The trustees should include description of voting behaviour during the year including the 'most significant votes'. Better IS's will break down voting statistics into type of issue.
- It is desirable that the most significant votes are aligned with schemes' stewardship priorities. Where trustees use a manager's policy, they should summarise whether the managers' voting behaviours were aligned with the trustees' own priorities.
- Trustees should include a brief reason in the IS for why a vote has been categorised as most significant, what the vote was, and why the scheme voted in the way it did. Trustees should explain whether, and how, they made clear to their managers what they considered to be the most significant votes in advance of those votes being taken.
- Where the trustee has set an expression of wish on voting in relation to any particular investment held, they should indicate in the IS whether this has been taken into account by their asset manager.

### Engagement

- Shareholder engagement is highlighted as a key stewardship tool which can take place over varying timeframes, working towards key milestones.
- In the IS, the Trustees could include details of engagement objectives, examples of engagement with asset managers and companies/issuers, how engagement has differed between different funds and where engagement has been escalated.

*The Statutory Guidance extends the governments growing focus on stewardship, setting out how they expect pension scheme trustees to take ownership of stewardship policies, engage with asset managers and report through the IS. Training on the requirements of this guidance should be a focus for trustees over coming months and trustees should consider identifying appropriate stewardship policies or themes to form a basis for future engagement and monitoring. Trustees can consider our [stewardship guide](#) as a starting point.*



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