

# Risky business: Local government pension funds and the climate crisis

How Local Government  
Pension Funds  
are failing to protect themselves  
from the **financial risks**  
of climate change.



## Executive Summary

Local government pension funds have a duty to act in their members best interests. This is secured both by ensuring financial performance and by acting in the best interests of the society at large.

Climate change will cause unprecedented loss of life and as such it is in the best interests of us all to address it. Climate change also poses economic threats both by altering environmental conditions and by demanding changes to the structure of the economy, as established by the Bank of England and the Environmental Audit Committee. In response the UK government is now proposing new legal duties for pension funds regarding climate change risks.

Past assessments have shown that the Local Government Pension Scheme (LGPS), administered in 97 local authorities, is heavily invested in fossil fuel companies, whose businesses practices are driving climate change. This analysis considers if this is symptomatic of a wider failure to take climate change seriously within the LGPS.

A framework for best practice was established by taking evidence from industry consultants and advisors, including Mercer, the Local Authority Pension Fund Forum, and Hymans Robertson. It was found that funds should be:

- Assessing and measuring climate risks in their portfolio.
- Managing them by divesting from /reducing exposure to high-risk companies and investing in low-carbon.
- Engaging with companies who can improve performance.
- Enshrining their commitment in clear and transparent policy and strategy.

Using this framework, we evaluated how seriously the largest LGPS funds were taking climate change across five areas:

1. Is climate change acknowledged as a material financial risk?
2. Are climate risks being measured as part of a coherent climate strategy?
3. Has a commitment been made to reduce investment in high risk companies, such as those involved in fossil fuel production?
4. Have clear goals been set for engagement with companies on climate change?
5. Are there investments in renewable and green technologies?

The report found:

- 8 funds are taking no or *almost* no action to protect their members from the financial risks posed by climate change. These funds are Hampshire, Essex, Kent, Hertfordshire, Tyne and Wear, Nottinghamshire, East Riding and Rhondda Cynon Taf.

- 5 funds acknowledge climate risks but are not acting to address them adequately. These are Lothian, West Midlands, West Yorkshire, Strathclyde and Northern Ireland.
- 2 funds are developing strategies to tackle climate change risks, but their actions are too heavily focussed on shareholder engagement without meaningful goals, deadlines or consequences. These are Greater Manchester and South Yorkshire.
- 4 funds are developing stronger climate change strategies including tilting or partial divestment from fossil fuels *as well as* engagement, and/or have engagement activities with clearer goals and timelines. These are Merseyside, Lancashire, London and Avon.

The majority of funds assessed explicitly state that climate change is a material financial risk. Kent was the only fund to state that climate change is not a financial risk. Despite this, over 50% of the funds have not measured climate risks and the majority of funds do not have explicit strategies for dealing with these risks.

A small minority of funds – Merseyside, London and Avon – are reducing their risk exposure by reducing their exposure to fossil fuel companies. Some funds are applying ‘tilts’ away from fossil fuel or are considering setting fossil fuel divestment targets.

Many of the funds assessed claim to use shareholder engagement with companies to address climate change but most of these funds do not have clear goals or targets for this engagement. No fund was able to provide evidence for the effectiveness of their engagement at forcing fossil fuel companies to switch their core business models away from fossil fuels.

A majority of funds have some low carbon investments, but the size of such investments varies.

**Overall, we conclude that the largest UK local government pension funds are failing to act effectively on climate change and are not properly accounting for the risks it poses.**

The assets under management of the funds assessed were £148 billion and constitute approximately half of the value of the entire LGPS. As such they give a strong indication that climate change is not being adequately addressed within the wider LGPS. This should give serious concern to pension funds, local councillors and the 6 million fund members who rely on the LGPS for security in retirement.

A set of questions for pension funds to answer is included in the report.

## Introduction

Climate change is one of the greatest challenges facing humanity and is already destroying lives and livelihoods. Climate change also presents multiple financial risks to investors. Fiduciary duty is now driving investors to address this risk. A growing number of investors are divesting from fossil fuel companies in order to protect their assets from growing financial stress in the gas and oil industry and align themselves with the Paris Climate Agreement.

The financial risks to pension funds from climate change are growing every year. The pressure to address these risks – from government, the Bank of England and from local people<sup>i</sup> and politicians – is also increasing. Some funds are starting to act, and protect themselves, but others lag way behind. This report looks at 19 large UK local government pension funds and assesses and ranks which funds are doing best – and worst.

It offers a series of questions that councillors, pension fund members and local people could ask their pension fund about climate change risks, to help ensure people's savings are protected.

## Background

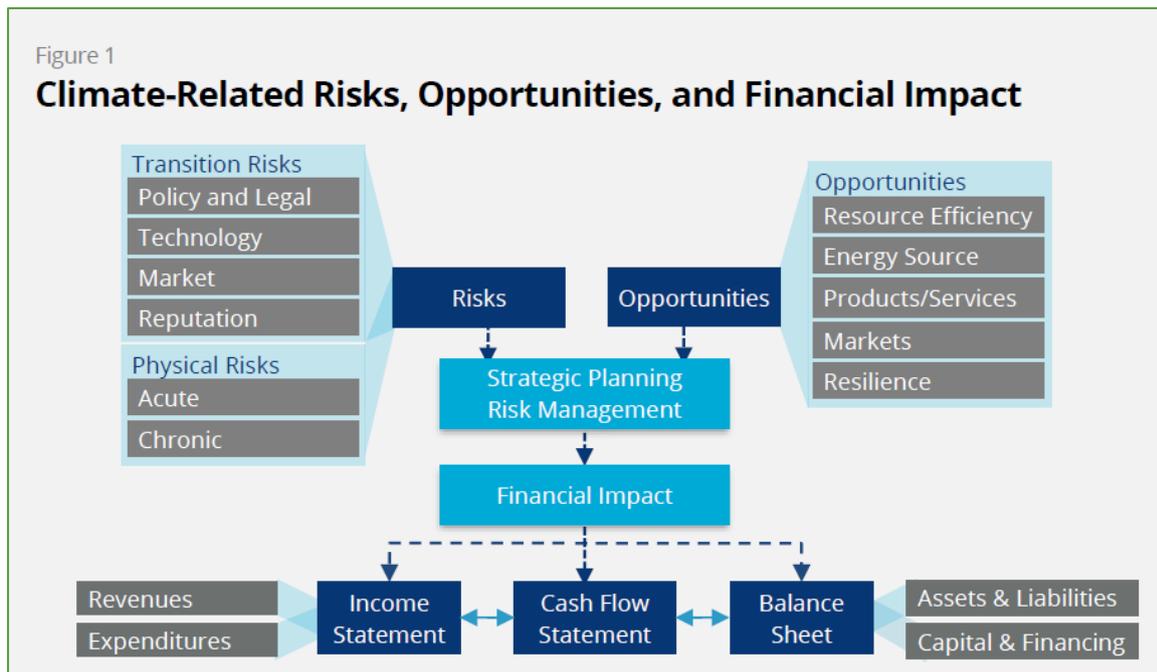
The government's new June 2018 consultation on clarifying and strengthening pension fund trustees' investment duties<sup>ii</sup> states that "*climate change is a financially material risk to our future*", and it is proposing that pension funds be required by law to state their policy to deal with these risks.

This builds upon the Bank of England-led "Task Force on Climate-related Financial Disclosure"<sup>iii</sup> framework (Figure 1) – there is now a growing acceptance that pension funds need to have strong governance structures to address climate change, involving assessment of the risks faced, and a strategy with targets and reporting to manage those risks. How pension funds tackle climate change is under increasing scrutiny, for example the UK's Environmental Audit Committee report on Greening Finance<sup>iv</sup> in 2018.

There are multiple climate risks that funds face, the two main groups are:

- **Transition risks:** the risks that funds face from potential loss of value to their holdings in companies in sectors such as fossil fuel production, which will undergo major transitions as the world moves to reduce its greenhouse gas emissions in line with the Paris Climate Agreement's net zero emissions goal.
- **Physical risks:** the risks to the whole fund or sectors within it from damages caused to global, regional and national economies from accelerating climate impacts (floods, storms, drought, crop-failure, mass-migration, sea-level rise, risks of tipping points being crossed).

**Figure 1: Task-Force on climate-related financial disclosures – assessment of types of climate risk:**



[Source: Recommendations of the Taskforce on Climate-related Financial Disclosures, June 2017, p8]

## Our Research

Friends of the Earth looked at 19 large UK Local Government Pension Funds<sup>v</sup> to assess how they are dealing with these climate risks. It is a mixed picture. This assessment comes in the context of the ongoing process of pooling of funds in England and Wales<sup>1</sup>. This process is occurring at different speeds in different regions, and in different ways. However, there is a general expectation that, although individual funds set policy, pools in many cases will implement it.

This report is structured in three parts:

- Part 1, a look at best practice guidance from industry professionals on how to address these risks.
- Part 2, an assessment of how 19 large UK Local Government Pension funds are performing against this guidance. -
- Part 3, a suggestion of questions which pension fund trustees, councillors and local people could ask their boards – to protect themselves and their funds from the growing financial risks from climate change.

Table 1 summarises the relative ranking of the funds in this report.

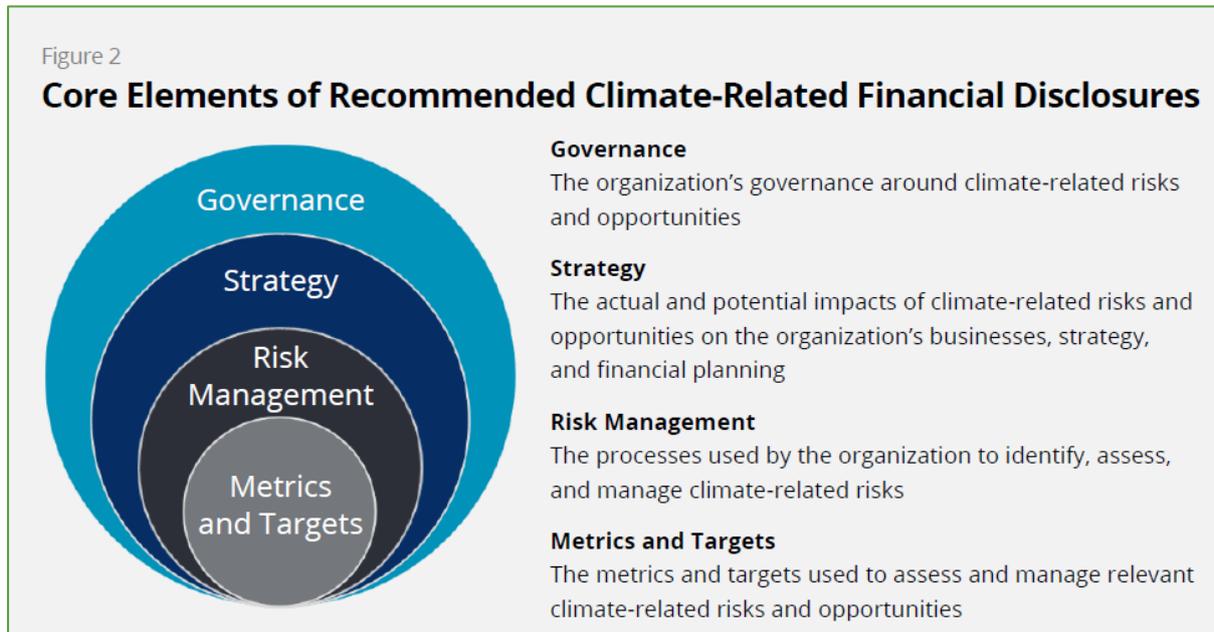
<sup>1</sup> A process underway where the 89 England and Wales local authority funds are merging into 8 “pools” of varying sizes: e.g. the Northern Pool comprises just 3 (Merseyside, Greater Manchester and West Yorkshire) and the London CIV has XX.

**Table 1: Summary of 19 large UK local government pension funds’ action to reduce the financial risks of climate change:**

<b>CATEGORY 5:</b> Laggard	<b>CATEGORY 4:</b> Aware, but taking inadequate action	<b>CATEGORY 3:</b> Some partial actions	<b>CATEGORY 2:</b> Acting at a number of levels	<b>CATEGORY 1</b> Leader
Kent Essex Rhondda Cynon Taf Hampshire Hertfordshire Tyne and Wear Nottinghamshire East Riding	West Midlands Lothian West Yorkshire Northern Ireland Strathclyde	Greater Manchester South Yorkshire	Merseyside London Avon Lancashire	None
<p>Response:</p> <p>It is urgent that these funds put in place a strategy to deal with climate change. Some of these funds do not yet acknowledge that climate change poses financial risks to the fund. Their failure to act is a breach of their fiduciary duty</p>	<p>Response:</p> <p>These funds are taking some action, but these are heavily reliant on unclear or ineffective engagement strategies. These funds need to expand out of their overly narrow focus on engagement, and also ensure that engagement activities have clear goals and deadlines. These funds’ failure to address climate risks adequately puts them at serious risk of breaching their fiduciary duty.</p>	<p>Response</p> <p>These funds have a broader strategy to address climate change risks, but these are still heavily dominated by engagement approaches</p>	<p>Response:</p> <p>These funds are starting to reduce their exposure to carbon risks via tilts or divestment, and/or are starting to set clearer deadlines and goals for their engagement strategies.</p>	<p>Response:</p> <p>Funds in this category are taking a range of strong actions with targets and deadlines, aimed at reducing financial risks to the fund and promoting a faster transition to a low-carbon economy.</p>

## Part 1- Addressing the financial risks of climate change;

The Task-Force on climate-related financial disclosures sets out a framework for addressing climate-related financial risks:



**Figure 2: Core elements of recommended climate-related financial disclosures.** [Source: Recommendations of the Taskforce on Climate-related Financial Disclosures, June 2017, page v]

Actions for pension funds to deliver on this framework include:

- Assessing risk:
  - Does the governance of the fund have a mechanism for ensuring climate risks are addressed: e.g. is it part of the Investment Strategy Statement (ISS)<sup>2</sup>?
  - What measurement and reporting does the fund do of the climate risks to the fund? E.g. carbon foot-printing is a start but has major methodological issues, and assessing companies' exposure to potentially stranded assets, and portfolio scenario analysis are stronger approaches.
- Managing risk:
  - Does the fund have a strategy for managing the climate risks to its portfolio?

Best-practice to manage climate risks is evolving, but there are three main areas:

- Reducing exposure to companies exposed to transition risk, such as fossil fuel companies.
- Allocations to low-carbon investments – to benefit from the transition to a low carbon economy and reduce likelihood of systemic risks.

<sup>2</sup> This ISS is a requirement in England. Equivalents outside England include Statements of Investment Principles.

- Climate engagement programs – to attempt to persuade companies, governments, regulators, service provider and peers to change their behaviour in order to reduce physical, transition and systemic risks.

On managing risks, these three areas are highlighted by Mercer (advisors to 18 LGPFs), Hymans Robertson (advisors to 25 LGPFs) and the Local Authority Pension Fund Forum (with 73 LGPF members):

**Mercer<sup>vi</sup>:**

*“Portfolios:*

*Reduce risk exposure in listed/unlisted holdings*

*Allocate to new opportunities*

*Engage directly and via managers”*

**Hymans Robertson<sup>vii</sup>:**

*“What actions can be taken to mitigate carbon risk. Having identified both the contributors to risk and the potential impact on returns arising from these assets, investors are typically faced with one of three possible courses of action, noting that these actions are not mutually exclusive:”*

- *Divest*
- *Tilt*
- *Engage*

**Local Authority Pension Fund Forum guidance to funds<sup>viii</sup>:**

*“We aim to integrate climate change considerations into the Investment Strategy in a number of ways, as follows:*

*Asset Allocation. We will consider a range of alternative investment strategies available to manage risks and opportunities related to climate change. These may include active management of carbon risk which results in some reduction of exposure, such as a tilt towards low carbon companies and assets, alongside company engagement and an increased allocation to low-carbon investment opportunities.”*

These three approaches to managing risks are general, and to an extent overlapping. A critical step – in line with the TCFD recommendations – is to set targets and goals for this risk management. This approach is exemplified by the Environment Agency Pension Fund<sup>ix</sup>:

*“We have set three targets for 2020:*

- ***Invest 15 per cent of the fund in low carbon, energy efficient and other climate mitigation opportunities.***
- ***Decarbonize the equity portfolio, reducing our exposure to “future emissions” by 90 per cent for coal and 50 per cent for oil and gas by 2020 compared to the exposure in our underlying benchmark as at 31 March 2015.***

- **Support progress** towards an orderly transition to a low carbon economy through actively working with asset owners, fund managers, companies, academia, policy makers and others in the investment industry.”

**Overall, best practice on climate change risks involves:**

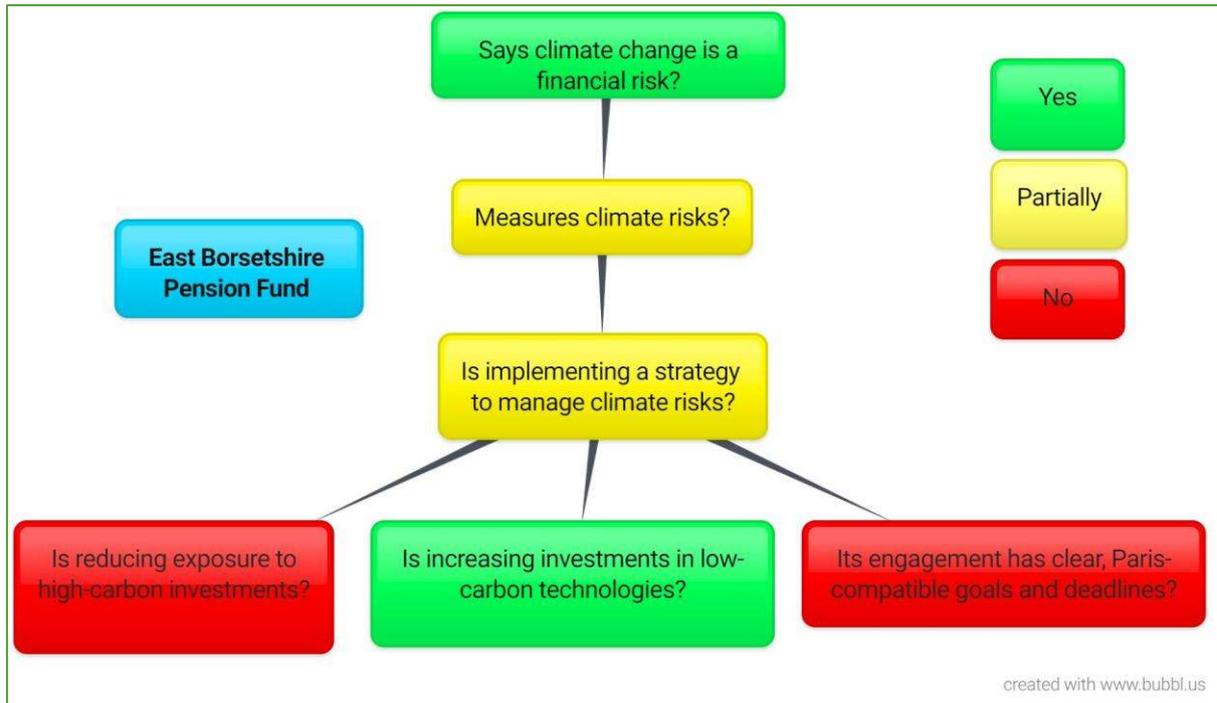
Assessment:

- A clear statement in the Investment Strategy Statement (or equivalent) that climate change constitutes financial risks to the fund.
- Measurement of risks – e.g. carbon reserve analysis, scenario analysis, and reporting to measure those risks
- A clear strategy with targets to manage those risks:

Management:

- Reduce risk exposure:
  - Divestment from high risk companies, such as fossil fuel extraction companies (steps towards this are tilting to reduce exposure to fossil fuels but not guaranteeing 100% exclusion (e.g. Environment Agency Pension Fund) or moving most of the assets to a fossil free fund but leaving some in a regular fund, (e.g. Hackney Local Government Pension Fund).
- Engagement:
  - Focus engagement on sectors where meaningful progress is possible – e.g. automotive, UK government, power – rather than ones where it is very unlikely (e.g. fossil fuel extraction)
  - Set clear engagement goals and timetables, and consequences if not successful;
    - E.g. the approach of the Church of England in July 2018<sup>x</sup>
    - The Oxford Martin Smith School have set 3 principles for “climate-conscious investment” covering long and short term-targets, and a net-zero business model<sup>xi</sup>.
- Reinvestment:
  - Set clear goals to reinvest in the renewable energy sectors as part of low-carbon transition.

**Figure 3: Flow-chart of elements of climate change risk management for an example pension fund:**



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## Part 2 – Local Government Pension Fund performance on addressing climate risk

We assessed 19 Local Government Pension Funds against 5 questions:

- 1) Does the Investment Strategy Statement say climate change is a material financial risk?
- 2) Are these risks then assessed (e.g. what proportion of a company's fossil fuel reserves are likely to be stranded), and is there a clear strategy for managing these risks?
- 3) Is there any reduction of risk exposure via divestment out of stocks with higher transition risks, such as fossil fuel production and exploration companies, or tilts away from high carbon investments?
- 4) What is the fund's approach to engagement? Are there any clear goals and deadlines for engagement, and escalation strategies if goals and deadlines are not met?
- 5) Is there any investment in the low-carbon transition?

### **1) Does the Investment Strategy Statement say climate change is a material financial risk?**

The majority of funds explicitly state that climate change is a material financial risk.

Some funds say that ESG issues can present financial risks, and climate change is an example of an ESG issue (e.g. Tyne and Wear).

Some funds do not mention climate change as a financial risk (e.g. Rhondda Cynon Taf).

One fund explicitly states that climate change is not a financial risk (Kent).

### **2) Are these risks then assessed and is there a clear strategy for managing these risks?**

A minority of funds assess/measure climate risks via some form of carbon foot-printing exercise. There is a common issue that such exercises do not include "scope 3" emissions, which account for the majority of emissions from fossil fuel production companies.

Most funds have no strategy for dealing with climate change risk, other than to say that they are involved in some form of engagement.

Almost half of the funds have some form of strategy that extends beyond engagement, for example measuring and foot-printing (Strathclyde, West Yorkshire), "tilts" away from fossil fuel investments (South Yorkshire, Avon, Merseyside), long-term goals (Greater Manchester) or as-yet-unimplemented aims to reduce fossil fuel exposure (West Yorkshire). Some funds say that they will develop and implement a strategy on climate change or are in the process of doing so (London, Lancashire). Some funds have explicit climate change strategies already in place (e.g. Merseyside, South Yorkshire).

**3) Is there any reduction of risk exposure via divestment out of stocks with higher transition risks, such as fossil fuel production and exploration companies, or tilts away from high carbon investments?**

Only a small minority of funds – Merseyside, London and Avon are reducing their fossil fuel exposure. Some say that they will do (West Yorkshire). South Yorkshire says it has introduced a tilt away from fossil fuels to its portfolio which is reducing its carbon footprint. Greater Manchester says that it is developing an approach to reduce the exposure of its passive investments to carbon emissions and intensity within the next financial year.

It is worth noting that several smaller Local Government Pension Funds, which were too small to be included in the scope of this study, have taken stronger action to protect themselves from exposure to fossil fuel companies. For example, Waltham Forest, Southwark and Islington Local Government Pension Funds have committed to divest from all fossil fuels while Hackney, Haringey and the Environmental Agency Pension Fund have made partial commitments to divest from fossil fuels.

**4) What is the fund's approach to engagement? Are there any clear goals and deadlines for engagement and escalation strategies if goals and deadlines are not met?**

A majority of funds claim to use engagement, either directly or outsourced to professionals, or via lobbying bodies (LAPFF). Some funds who do engagement do not focus on climate change (Strathclyde). A large minority of funds do not mention engagement at all.

Funds tend to focus engagement on companies, although some engage with governments via the Institutional Investors Group on Climate Change (IIGCC). Engagement with fossil fuel exploration and production companies has been unsuccessful in delivering meaningful progress, for example getting those companies to align their business models with the Paris Climate Agreement goals<sup>xii</sup>. Funds have limited engagement capacity and should focus it on areas where meaningful progress is possible – for example the automotive or electricity sectors, or engagement with national policy makers.

Very few funds set out any goals or deadlines for their engagement. As such it is not clear on what basis they believe that this open-ended engagement is or can be effective in protecting themselves from either transition or systemic climate risks. Some funds state that their engagement is effective (West Yorkshire, South Yorkshire), but as there are no criteria set, this is hard for them to justify. Objective external evaluation (e.g. from Schroders<sup>xiii</sup>, ShareAction<sup>xiv</sup>) would say that the actions of companies such as Shell and BP are not compatible with the Paris Climate Agreement goals, and neither are they on a trajectory to become compatible.

Some funds (South Yorkshire, London, Lancashire) say that if companies “*fail to respond adequately*” to engagement overtures, then divestment would become an option. This is welcome acknowledgement that if engagement is not successful, other actions are required, however it is not clear what would constitute adequacy in the absence of specific timeframes and targets. These should be set.

## 5) Is there any investment in low-carbon transition?

A majority of funds mention investments in low-carbon. Some funds mention existing investments and planned increases, sometimes this is quantified. Some funds count investments by fossil fuel exploration companies in renewable technology as a success of their engagement, however when the overwhelming majority of these companies' investments are still in fossil fuels, this appears to be cherry-picking at best. For example, Shell's cleaner energy investments are predicted to be \$1-2 billion out of \$25-30 billion in 2018-2020<sup>xv</sup>.

One of the main purposes of the government's move to pooling pension funds was to facilitate greater pension fund investment in infrastructure. The low-carbon transition required to tackle climate change - protecting long-term pension fund value - will require a step-change increase in low-carbon infrastructure investment, a point made in this year's National Infrastructure Assessment<sup>xvi</sup> for the government. Pension funds have a role and interest in facilitating this investment. Conversely, funds should avoid investments in future new high-carbon infrastructure which is more likely to become stranded in future. Recent macroeconomic analysis has shown that even on just current trends for low-carbon technology diffusion, without additional climate policies, fossil fuel assets will be stranded<sup>xvii</sup>.

Table 2 below sets out an overarching summary and ranking of the funds' performance, and Table 3 sets out in summary how each fund is doing against the 5 questions. Details and references are set out in the appendix.

In summary, the Local Government Pension Funds examined can be split into four groups:

- First, there is a group of 8 funds who are taking no or almost no action to protect their members from the financial risks posed by climate change; urgent action is required to rectify this. This group comprises Hampshire, Essex, Kent, Hertfordshire, Tyne and Wear, Nottinghamshire, East Riding and Rhondda Cynon Taf.
- Second, there is a group of 5 funds who are acknowledging there are risks, but not acting to address them adequately. This group comprises Lothian, Strathclyde, West Midlands, West Yorkshire and Northern Ireland
- Third, there are 2 funds who are developing strategies to tackle climate change risks, but whose actions are too heavily focussed on engagement, and engagement without meaningful goals, deadlines or consequences. This group comprises Greater Manchester and South Yorkshire.
- Fourth, there is a group of 4 funds who are developing broader climate change strategies – who include tilting or divesting away from fossil fuel companies as well as engagement, and/or whose engagement activities have clearer goals and timelines. This group comprises Merseyside, Lancashire, London and Avon.
- None of the funds examined are currently in the “Leader” category, however the content of the imminent publication of changes to London's LPFA climate policy may move London into this category.

**Table 2;**

**Summary of 19 large UK Local Government Pension Funds’ action on financial risks of climate change:**

<b>CATEGORY 5:</b> Laggard	<b>CATEGORY 4:</b> Aware, but taking inadequate action	<b>CATEGORY 3:</b> Some partial actions	<b>CATEGORY 2:</b> Acting at a number of levels	<b>CATEGORY 1</b> Leader
Kent Essex Rhondda Cynon Taf Hampshire Hertfordshire Tyne and Wear Nottinghamshire East Riding	West Midlands Lothian West Yorkshire Northern Ireland Strathclyde	Greater Manchester South Yorkshire	Merseyside London Avon Lancashire	None
<p>Response:</p> <p>It is urgent that these funds put in place a strategy to deal with climate change. Some of these funds do not yet acknowledge that climate change poses financial risks to the fund. Their failure to act is a breach of their fiduciary duty</p>	<p>Response:</p> <p>These funds are taking some action, but these are heavily reliant on unclear or ineffective engagement strategies. These funds need to expand out of their overly narrow focus on engagement, and also ensure that engagement activities have clear goals and deadlines. These funds’ failure to address climate risks adequately puts them at serious risk of breaching their fiduciary duty.</p>	<p>Response</p> <p>These funds have a broader strategy to address climate change risks, but these are still heavily dominated by engagement approaches</p>	<p>Response:</p> <p>These funds are starting to reduce their exposure to carbon risks via tilts or divestment, and/or are starting to set clearer deadlines and goals for their engagement strategies.</p>	<p>Response:</p> <p>Funds in this category are taking a range of strong actions with targets and deadlines, aimed at reducing financial risks to the fund and promoting a faster transition to a low-carbon economy.</p>

**Table 3: Funds' approach to addressing climate change risks:**

	Says climate change is a financial risk?	Has measured climate risks and has a strategy?	Moved any investments out of fossil fuels?	Has goals/targets for its engagement?	Invests in low-carbon?
Strathclyde	Yes	Measures footprint, but flawed process. Has a strategy.	No	No	Yes. Is increasing its low-carbon investments
Greater Manchester	Yes	Some foot printing. Strategy is evolving, and has goals, e.g. an undated target of Paris-compliance	Developing an approach to reduce exposure, of £2 billion of its passive investments, to carbon emission and intensity within the next financial year.	No	Yes. These investments are increasing. Plus, investments via consortium with other funds
West Midlands	Yes	No measurement. No explicit strategy; has focus on engagement only	No	No	Has invested in renewable energy. Invested £100m in a windfarm in Scotland in August 2018.
West Yorkshire	Yes	Has committed to measure and reduce exposure, but not either yet. Focus is on engagement	No	No	Yes. £275m plus investments via consortium with other funds
Merseyside	Yes	Yes to both	A tilt of its passive holdings out of fossil fuels	No	Yes, £184m plus investments via consortium with other funds
Tyne and Wear	No. Says CC is an ESG issue	No. Delegates the issue to investment managers.	No	No	Some unquantified investments are mentioned
South Yorkshire	Yes	Yes. Has a strategy	Not invested in coal. Says a tilt away from fossil fuels is being applied	Says it will reduce exposure to companies failing to respond, but has not clear deadlines or goals	Some unquantified investments are mentioned
Lothian	Yes, very recently	Has done some foot printing	No	No	£113m invested in renewables

Lancashire	Yes	A strategy is in draft, due Dec 2018	Will not consider new investments in fossil fuel companies ignoring risks of climate change. Considering divestment target.	Intend to divest from companies failing to respond	Yes, although funds' climate-related materials don't mention it
Hampshire	No. Says CC is an ESG issue	No	No	No	Not mentioned
Essex	Not mentioned	No	"Goes against fiduciary duty"	Not mentioned	Some unquantified investments in wind/solar are mentioned
London	Yes	Yes	No new investments in fossil fuels, looking at divesting existing holdings	Will divest if no progress. But 'no progress' not defined	Yes, plus investments via consortium with other funds
Nottinghamshire	Yes	No	"Engagement not negative screening"	No	Not mentioned
East Riding	Yes	No	No	Not mentioned	One very small holding
Kent	Explicitly says not a risk	No	No	No	Have up to £43m in low-carbon technologies
Avon	Yes	Carbon foot printing in progress. Strategy evolving	Passive equities switched to low carbon fund	No	Yes, up to 7.5% of assets
Hertfordshire	Financial risks from ESG issues	No	No	No	Not mentioned
Northern Ireland	Yes	No measurement. Some elements of a strategy, heavily dominated by engagement.	No	No	Some unquantified investments + "proactive consideration" of more
Rhondda Cynon Taf	Not mentioned	No	No	No	Not mentioned

## Part 3: Questions trustees, councillors, pension fund members and local people could ask their pension fund:

This section sets out a series of questions which councillors, pension fund managers and local people could ask a pension fund which is pursuing a narrow, engagement-only strategy. It also sets out some questions regarding the other issues in this briefing – risk reduction, low-carbon investment, and assessing risk.

Many pension funds state that engagement is sufficient to manage climate change risks. The flaws with the arguments used to justify such an approach are covered in more detail in a separate March 2018 briefing<sup>xviii</sup>.

### Questions to ask pension funds:

#### Assessing risks and strategy-setting:

- *What advice have you sought on climate risks, and when? Do your mandates and contracts with advisors reflect the necessity to consider climate risks, and how often are you updating this advice?*
- *Will you commit to implementing a comprehensive risk assessment and management strategy to protect the fund from the multiple risks posed by climate change?*
- *Will you ensure that assessment of climate risks posed by companies looks at scope 3 emissions (those caused by the use of the company's product), not just scope 1 and 2 (those emitted in making the product)?*

#### Reducing risk exposure:

- *Will you commit to timetabled reductions in exposure to companies involved in continued exploration and production of new fossil fuels? Such new production would breach the Paris Climate Agreement goals, threatening the financial stability of the fund.*
- *If you state that there are financial risks which are preventing you from divesting fossil fuel stocks, will you publish your analysis of what these risks are<sup>3</sup>?*
- *Will the fund produce and implement an analysis of how it could meet its obligations without investments in risky fossil fuels?*
- *Has the fund assessed whether the fossil fuel majors' forecasts for future fossil fuel demand are accurate? What is the fund's view on these companies' consistent under-forecasting over the last decade of renewable energy growth?*

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<sup>3</sup> Some funds state assert that there are financial risks from divestment. On the “mythical peril” of divesting, see this June 2018 article from the Grantham Institute: <http://www.lse.ac.uk/GranthamInstitute/news/the-mythical-peril-of-divesting-from-fossil-fuels/>

- *What is the fund's response to the March 2018 Carbon Tracker report<sup>xix</sup> that trillions of dollars of fossil fuel capital expenditure are at risk if the world moves onto a <2 degree trajectory, compared to the 3+ degree trajectory that Shell and BP use as their central planning scenario?*

#### Engagement with fossil fuel companies:

- *Has the fund conducted analysis of where it can most effectively use its limited capacity for engagement on climate change issues?*
- *What are the current goals of your engagement with BP and Shell and other fossil fuel companies? Is engagement with these companies being pursued by the fund as a risk-reduction strategy? If so, what specific measures are you asking for, what timeframes are you giving companies to implement them, what assessment have you made of these companies' progress to date, and what will you do if they do not act?*
- *Have you assessed whether you are in breach of your fiduciary duties if you hold fossil fuel stocks, knowing the financial risks?*
- *What climate shareholder resolutions are you supporting? Have you assessed whether these motions if passed would constitute a Paris-compliant strategy from the company in question?*
- *We believe that a Paris-compliant strategy for a fossil fuel company would be to commit to no new fossil fuel capital expenditure by the end of 2019, a managed decline in production, and to reduce overall GHG footprint to zero by 2050 (scope 1,2,3), with compatible interim milestones for 2025, 2030 and 2040. Will you commit to strengthening your engagement strategy in line with these goals and deadlines, and divest if companies do not set these goals?*
- *Will the fund commit to setting a rapid "end-game" situation for its engagement with fossil fuel companies, and if these companies do not respond, divest and redirect its engagement resources into engaging with government and companies in automotive, electricity and heavy energy-using sectors?*

#### Low-carbon investment:

- *Keeping the world below 2 degrees is a \$12 trillion investment opportunity according to Bloomberg and CERES<sup>xx</sup>. We support efforts to increase the percentage of cleaner investments; we consider this to be an essential element of a comprehensive strategy to protect funds from climate change risks. Will the fund commit to increasing its share of low-carbon and renewable investments?*

## Appendix: Analysis of individual pension funds.

A 1-4-page analysis of the actions for each of the 19 funds considered in this report is found in a separate appendix, available at <https://tinyurl.com/y8x75h9d>

### Disclaimer:

This report is intended for information purposes only; the authors of this report cannot provide financial product advice. The report is not a guide to investment, nor a source of specific investment recommendations. The information contained in the document was compiled from sources that we believe to be reliable, but accuracy cannot be guaranteed, and the information is provided with the understanding that we are not engaged in providing legal, accounting, financial advisory or tax services. We recommend that all investors seek out the services of competent professionals in the relevant area(s) prior to making investment decisions.

### References:

<sup>i</sup> <https://www.professionalpensions.com/professional-pensions/news/3061348/savers-expect-pension-funds-to-avoid-fossil-fuels-finds-poll>

<sup>ii</sup> <https://www.gov.uk/government/consultations/pension-trustees-clarifying-and-strengthening-investment-duties>

<sup>iii</sup> <https://www.fsb-tcfd.org/wp-content/uploads/2017/06/FINAL-TCFD-Report-062817.pdf>

<sup>iv</sup> <https://publications.parliament.uk/pa/cm201719/cmselect/cmenvaud/1063/106302.htm>

<sup>v</sup> These are the top 17 funds by value, which is 2 Scottish and 15 English funds. Plus, for the 18<sup>th</sup> and 19<sup>th</sup> LGPFs studied we chose NILGSOC (21<sup>st</sup> by value) and Rhondda Cynon Taf (33<sup>rd</sup> by value), the largest Welsh fund, so there were funds assessed from each nation.

<sup>vi</sup> <https://www.mercer.com/content/dam/mercer/attachments/global/investments/long-term-investors-are-you-aware-of-your-climate-change-risk-exposure-mercer-2015.pdf>

<sup>vii</sup> [https://www.hymans.co.uk/media/uploads/150811\\_Investment\\_perspectives\\_FINAL.pdf](https://www.hymans.co.uk/media/uploads/150811_Investment_perspectives_FINAL.pdf)

<sup>viii</sup> LAPFF, 2017. Climate Change Investment Policy Framework. November.

<sup>ix</sup> <https://www.eapf.org.uk/investments/climate-risk/tackling-climate-risk>

<sup>x</sup> <https://www.businessgreen.com/bg/news/3035562/church-of-england-votes-for-oil-and-gas-divestment-push>

<sup>xi</sup> University of Oxford Oxford Martin School, 2018. [Principles for Climate Conscious Investment](#). February

<sup>xii</sup> See <https://www.friendsoftheearth.uk/climate-change/briefing-pension-funds-engagement-fossil-fuel-companies-march-2018> for further detail on pension funds' work on engagement with fossil fuel companies.

<sup>xiii</sup> <https://www.schroders.com/en/uk/pensions/insights/climate-progress-dashboard/>

<sup>xiv</sup> <https://shareaction.org/wp-content/uploads/2017/10/InvestorReport-AimingForA-Shell.pdf>

<sup>xv</sup> <https://www.theguardian.com/business/2017/nov/28/shell-doubles-green-spending-vows-halve-carbon-footprint>

<sup>xvi</sup> <https://www.nic.org.uk/publications/national-infrastructure-assessment-2018/>

<sup>xvii</sup> Mercure, et al, 2018. [Macro-economic impact of stranded fossil fuel assets](#). Nature Climate Change, 8, 588-593

<sup>xviii</sup> <https://www.friendsoftheearth.uk/climate-change/briefing-pension-funds-engagement-fossil-fuel-companies-march-2018>

<sup>xix</sup> <https://www.carbontracker.org/reports/mind-the-gap/>

<sup>xx</sup> <https://www.ceres.org/resources/reports/mapping-gap-road-paris>

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