The Greater Gwent (Torfaen) Pension Fund

administered by Torfaen County Borough Council

LOCAL GOVERNMENT PENSION SCHEME

Climate Change Policy

Introduction

Scientists have told us that the climate is changing, largely due to greenhouse gases such as CO_2 (carbon dioxide) increasing average world temperatures.

We invest pension fund savings money for the long-term. We believe that climate change is a large and material financial risk to all of our different investment assets all over the world, because:

- Climate change will cause physical risks, such as rising sea level, extreme weather events, extreme temperatures in parts of the world, and the effect these may have on resources, assets and supply chains.

- The response to climate change is to mitigate and adapt to climate change by transitioning to a low carbon economy; and recognise and manage the risks that come from the policy, legal, technology, and market changes that are needed to do this.

The most notable policy and legal developments to date include:

- The Climate Change Act 2008 (as amended), which sets out new UK government targets to cut CO_2 (carbon dioxide) emissions by 100% of 1990 levels by 2050.

- The 2015 Paris Agreement, which the UK government has signed up to.

This aims to decrease global warming and enhance the United Nations Framework Convention on Climate Change by:

(a) Holding the increase in the global average temperature to well below 2°C above pre-industrial levels and to pursue efforts to limit the temperature increase to 1.5°C above pre-industrial levels, recognizing that this would significantly reduce the risks and impacts of climate change;

(b) Increasing the ability to adapt to the adverse impacts of climate change and foster climate resilience and low greenhouse gas emissions development, in a manner that does not threaten food production;

(c) Making finance flows consistent with a pathway towards low greenhouse gas emissions and climate-resilient development.

- What is clear is that whilst government targets and legislation may change, the Fund must maintain an ambition and a clear path towards meeting government requirements as set out from time to time in legislation or guidance, and must therefore review and re-set this policy approach and the targets it aspires to periodically.

Our overall approach to Climate Change

We strive to be a responsible investor.

The financial risks of climate change have the potential to affect the beneficiaries of the Pension Fund, the LGPS members that we'll pay pension benefits to, and their dependents. The financial risks of climate change also have the potential to affect LGPS employers who pay contributions to underpin the pension benefits we pay to LGPS members.

We believe that considering and responding to climate risk is part of our fiduciary duty to act in the best interest of our beneficiaries. Our legal fiduciary duty means that we have to invest responsibly to help lower financial risk.

Our overall policy objective is to lower the 'carbon footprint' of the greenhouse gas emissions of our investments, so that we are either in line or, ideally, below the international targets to keep global warming well below 2°C. We recognise that government policy and legal requirements may change going forward. Therefore we look at the 2°C target as a current baseline objective and, taking a risk-based approach, we will aim to achieve well below 2°C.

Our policy objective is also to identify various investment risks and opportunities that will come from the transition to a low carbon economy.

- Risks may come in the form of companies unable to adapt in time make a smooth transition to a low carbon economy; carbon pricing policies which may lower investment returns; or from assets which may become stranded such as shares in fossil fuels which, to avoid further global warming, future legislation may prevent being burned.

- Opportunities may come in the form of technological changes, and companies that innovate, adapt and improve, including those producing low carbon energy and installing low carbon infrastructure.

Our Climate Change Policy Starting Point

There is currently no internationally agreed way of measuring the carbon footprint of investments. Our research shows there are various specialist advisors and a number of ways to assess and calculate carbon footprints.

In addition, various interest groups and bodies have reported on responsible investment in particular in respect of climate change. This has included, for example:

> (i) The Fuelling the Fire Report produced by a collective of climate interest bodies which reported the Fund as investing 9.1% of its assets (£245m) in fossil fuels as at March 2017. Since the original report was published, the value of the Funds' investments have increased by over 10%. Despite this, the actual sum invested has fallen to £208m (6.95% of total investments) as at April 2019. Whilst this is a positive step forward we recognise that we still have much to do. We are now working to reduce our carbon footprint further but in a planned and controlled way.
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> (ii) The "Responsible Investment in LGPS" report (April 2019) by Unison and Share Action that reviewed our investment strategy statement as it relates to various issues including climate change and gave us an overall ranking of "D" (Scale of A-E). This placed us with the same ranking as 50% of local authority pension funds.

We know that there are many different approaches to measuring the carbon footprint of investments and many different measurement providers; and that measurement may change over time to achieve greater consistency. We have taken specialist advice to measure the carbon footprint of our investments, and to assess the amount by which we would need to lower this over time, so that we would be in line with a below 2°C scenario.

Our advisors have used the way which appears to be the most comprehensive. That is the method suggested by the Task Force on Climate-related Financial Disclosures to use data from Scope 1, Scope 2 and, where available Scope 3. The Greenhouse Gas Protocol defines these as follows:

> **Scope 1 Emissions**: These are direct emissions (gas, heat, light etc.…that are sent out into the atmosphere) from a company's operational activities.
>
> **Scope 2 Emissions**: These are indirect emissions generated from the purchase of electricity.
>
> **Scope 3 Emissions**: These all other emissions over which a company has influence but not control over such as distribution of goods, transport, waste, commuting, business travel etc.…

We know that Scope 1 and 2 measurements are better developed and more widely calculated and assessed. Scope 3 however provides a more comprehensive picture but is much less well developed. The Fund will therefore use a range of calculations incorporating both approaches to assess and monitor its progress towards carbon reduction.

Our specialist advisers have told us in late 2018 that our carbon footprint is higher than we would like it to be, and that we are not currently in line with a below 2°C scenario. Since then, we have changed our investment manager for our global equity investments and also reduced the monies invested in UK companies, both of which have had a positive effect in reducing our carbon footprint. Further work is ongoing to continue to reduce our carbon emissions.

Short-Term Policy Steps to Lower our Carbon Footprint

- We believe that we need to make changes to our investments, and the types of assets that we invest in, to lower our carbon footprint in the short-term and put us on course towards achieving a below 2°C scenario.

- Before moving any money from a current investment we will, if possible, seek ways to measure what its potential carbon footprint would be in any suggested new investments; this is so that we can make an evidence-based decision before moving investments.

- We will work closely with the operator of the Wales Pension Partnership to ensure that pooled investments are available which will keep us on course towards achieving a below 2°C scenario.

- For investments that track indices, we will seek specialist advice on 'tilts' that avoid industries and companies with high carbon footprints. We will then make an evidence-based decision about moving investments into those tracking lower carbon indexes.

Medium to Longer Term Policy Steps to Lower our Carbon Footprint

Our aim is to fully integrate climate risk and opportunities into our investment strategy. We will do this by seeking specialist advice and undertaking further research:

- On potential secure long-term investments in companies that help mitigate the effects of global warming, and those that are innovating, adapting and improving on the transition to a low carbon economy, including those producing low carbon energy and installing low carbon infrastructure.

- On companies and industries that are high carbon emitters and how effectively they are transitioning to a low carbon future. We will use this to make evidence-based decisions on disinvestment.

- On assets which may potentially become 'stranded' on the transition to a low carbon economy. This may include investments in companies that are not transitioning effectively, or potential changes in carbon offsetting tax policy, or investments in companies producing fossil fuels which may potentially become stranded (non-burnable) due to tightening of policy or legislation. We will use this to make evidence-based decisions on disinvestment.

In support of the above, we have identified the following more specific immediate requirements:

1. Make clear and communicate more effectively our commitment and the actions we are taking towards carbon reduction.

2. Actively seek, research and consider investment opportunities aimed at reducing our carbon footprint.

3. Respond appropriately to changing government requirements and make clear our progress towards carbon neutrality.

4. Assesses our carbon footprint each year to show how we are lowering our carbon footprint.

5. Continue to monitor and assess the most appropriate measurement methods for assessing our carbon footprint.

6. Review fund benchmarks to make sure they remain appropriate for measuring that we are lowering our carbon footprint.

7. Ensure that we support the collective influence of the Local Authority Pensions Fund Forum, where we continue in the short-term to hold companies with higher carbon exposures.

8. Where our third-party investment managers invest our pension fund money directly in individual companies, we will challenge them on their choices and their measurement of the carbon footprints of these investments.

9. Contribute effectively to the Wales Pension Partnership investment collaboration to influence their approach to ESG generally and lowering their carbon footprint specifically.

We will continue to develop our Climate Change policy, based on our fiduciary duty to act in the best interests of our beneficiaries, towards ensuring that we invest Pension Fund money in sustainable and secure long-term investments.

Torfaen Pensions,
Resources Directorate,
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