ACTION FOR PENSION WEALTH AND PLANET HEALTH

2022 CANADIAN PENSION CLIMATE REPORT CARD

January 2023

EXECUTIVE SUMMARY

Canada's largest pension funds have an outsize role to play in protecting the retirement security of millions of Canadians from the financial risks of climate change and deploying pension capital to rapidly transform our energy systems and decarbonize the economy.

The climate crisis poses existential challenges for pension funds, from accelerating risks to individual investments and economic sectors to growing threats to the stability of the economic, ecological and financial systems on which retirement security depends. Meeting fiduciary obligations to invest responsibly over the long-term requires new and unprecedented changes to the way pension funds allocate capital, make investment decisions and manage assets. Financial institutions at every level are discovering just how steep the learning curve is for creating and implementing credible climate plans.

With this inaugural *Canadian Pension Climate Report Card*, Shift has established an independent benchmark for evaluating the quality, depth and credibility of pension fund climate policies based on the latest science and international best practice. Our goal is to educate pension managers, pension directors and trustees, plan members, sponsors and other stakeholders of progress to date, document specific challenges and shortcomings faced by individual funds and highlight best practices and emerging leadership. This report focuses on 11 of Canada's largest pension managers, including the so-called 'Maple 8', and includes examples of four international pensions for comparative purposes. This benchmark can be used to evaluate climate plans for all Canadian pension managers, which collectively manage over $4 trillion.

This report independently builds on and complements the *Canadian Pensions Dashboard for Responsible Investing*[1] and *Building Climate Resilience in Canada's Pension Funds*[2] reports, which use a wide range of sustainable finance metrics to quantitatively and qualitatively assess the climate and responsible investing approaches of major Canadian pensions, as well as providing important recommendations for improvement.

Shift reviewed pension fund climate strategies using a range of quantitative and qualitative indicators. Quantitative indicators are included in the report to provide general information and context for the authors' assessments, but were not directly factored into assigned scores. The qualitative indicators used to evaluate pension fund climate strategies are the basis upon which letter grades were assigned. They include:

- Credible Paris-aligned portfolio-level climate targets
- Ambitious and accountable interim climate targets
- The extent to which the pension manager is communicating the urgency and severity of the climate crisis
- The robustness of pension fund engagement programs, strategies and actions to align portfolio companies to climate targets
- The degree to which pension managers have integrated climate in investment strategy and decision-making across the organization
- Policies to exclude fossil fuels in recognition of financial risk and engagement limitations.

Pension Fund Climate Scores

For a detailed analysis of each fund and its scores, click on the fund's name in the table below. (Pension funds are ordered from best to worst score).

	OVERALL SCORE	Paris-Aligned Target	Interim Targets	Climate Urgency	Climate Engagement	Climate Integration	Fossil Fuel Exclusions
CANADIAN FUNDS							
CDPQ	B+	A–	B	A	B–	B	B–
OTPP	B	A–	B	A	B+	B–	F
UPP	B	A–	B–	A	B	B–	D+
IMCO	B–	B	B–	B+	C+	C+	D+
PSP	C	F	B–	B+	C	C+	F
CPPIB	C–	C	F	B	C+	C+	F
BCI	D+	F	D+	C+	C	C+	F
OMERS	D+	C	C	C+	D–	D+	F
OPTrust	D+	C–	D	C+	D	D	F
HOOPP	D	C–	D	C	F	F	F
AIMCo	D–	F	F	D+	D–	D	F
INTERNATIONAL FUNDS							
Nest	A–	B–	C+	A+	A	A–	B
AP2	B+	A–	C+	A–	B–	B	A
NGS Super	B	B–	C	A	B+	B–	B
NYSCRF	B	B–	C	B	A	B–	C+

Key Findings

- **Not yet climate-aligned.** The climate plans of Canada's largest pension funds are not yet aligned with the path required to protect the retirement security of beneficiaries while ensuring a safe climate future.
- **Signs of progress.** The majority of Canada's largest pension funds have made measurable progress in recent years in developing investment strategies that address the risks and opportunities of the global climate crisis, but far more is needed.
- **Significant variability.** The degree of urgency, detail, transparency, rigour and ambition of approaches for managing climate-related risks and opportunities varies significantly.
- **Lack of transparency.** While disclosure of climate-related financial risks has improved over time, it remains impossible for beneficiaries and stakeholders to properly assess the degree to which beneficiaries are exposed to climate risks based on the information publicly disclosed by their pensions.
- **Lack of interim targets.** The majority of Canadian pension funds do not have meaningful interim emissions reduction targets.
- **No absolute emissions targets.** No Canadian pension fund has adopted portfolio-wide absolute emissions reduction plans.
- **The black box of Scope 3 emissions.** Just one Canadian fund has reported the scope 3 emissions associated with its oil and gas and mining assets; no other fund has reported any financed scope 3 emissions.
- **Engaging with low expectations, few consequences, and no timelines.** Canadian pension strategies for climate engagement with owned companies lack the transparency, rigour, expectation-setting and escalatory measures required to align business models with a path to zero emissions and climate stability. This finding is particularly problematic in relation to Canadian pension funds' ongoing intention to engage with fossil fuel companies, for whom there are no credible pathways to decarbonization other than phase-out.
- **Early signs of climate integration.** Canadian pension funds are increasingly using sophisticated tools to ensure the management of climate risk is integrated across their investment decision-making and asset management processes, including 1.5°C-aligned scenario analysis and financed emissions measurement. Funds are also developing overlapping governance and portfolio management structures that infuse climate risk across the organization, and providing climate-related training and education for staff and directors/trustees. At least two funds have drawn a link between compensation and the achievement of climate targets, a practice that all Canadian funds should adopt.
- **A Canadian reluctance to admit that fossil fuels lack credible climate-aligned pathways.** A significant gap has emerged between Canadian pension funds and leading global institutional investors in their approach to fossil fuels. While climate-leading investors have explicitly recognized the urgent imperative of a rapid phase-out of fossil fuels, many Canadian pension sector leaders cling to an unfounded belief that ongoing investment in oil and gas is somehow part of the energy transition.
- **Greenwashing is commonplace.** Canadian pensions consistently tout their commitment to climate action and Paris-alignment without having made the investment, asset management and stewardship decisions necessary to follow through. For example, many pension managers frequently fail to consistently define and disclose what they consider to be "green assets" vs. "transition assets", thereby undermining their pledges to allocate capital to real climate solutions. Shift has assigned a bronze, silver, and gold "Greenwashing Award" to three Canadian pension funds for making investment activities appear to be more

environmentally friendly or less environmentally damaging than they really are. PSP Investments is awarded the Bronze Star, Ontario Teachers' Pension Plan the Silver Star, and CPP Investments the Gold Star for greenwashing.

- **Lack of Indigenous rights and reconciliation frameworks.** It appears that only a handful of pensions covered in this report have taken steps to develop an Indigenous rights and reconciliation framework in their investment processes, including transparent policies to respect the rights of Indigenous Peoples in investment decisions. The United Nations Declaration on the Rights of Indigenous Peoples (UNDRIP) explicitly requires Free, Prior and Informed Consent (FPIC) for activities that may affect Indigenous Peoples or their territories.

Recommendations

The full participation of financial institutions in climate action is inevitable, both to protect the funded status of pensions, and to prevent a worsening global catastrophe. There is no justification for further delaying action to develop and implement credible climate plans.

This report offers comprehensive recommendations for pension managers, trustees and directors to assess their own management of climate-related risks against best practices for setting short-, medium- and long-term Paris-aligned targets, communicating climate urgency, developing and implementing a robust climate engagement program, infusing the management of climate risks across the organization, and protecting beneficiaries from the unique financial risk profile of the fossil fuel industry. It also includes some recommendations and resources to assist pension funds in developing an Indigenous rights and reconciliation framework. Although comprehensive recommendations for the development of federal and provincial laws, regulations and policies to align Canada's financial institutions with a safe climate future is outside of the scope of this report, the inadequacy of pension fund climate strategies underscores the need for legislative and regulatory reform.

More action on board-level climate governance is also needed from pension fund sponsors and trustees. Climate-related expertise and experience should be a required competency for corporate directors, especially in the governance of pension funds, which have a long-term investment horizon and a fiduciary duty to invest in the best interests of plan members, young and old.

The fossil fuel entanglement of some pension boards is a growing concern, as it creates the potential for conflicts of interest in climate-related decision-making. Ongoing pension board entanglement with fossil fuel companies could delay or impede important decisions required to protect the fund from climate-related financial risks. Fossil fuel entanglements should be avoided for new director appointments.

Adopting credible climate plans is not easy. The climate crisis presents an unprecedented challenge for pensions. No pension fund climate plan will ever be perfect, but all funds must get started with Paris-aligned plans now. Institutions that develop internal expertise, capacity, experience and a culture of experimentation are likely to be rewarded in the long-term.

ENDNOTES

1 Smart Prosperity Institute, The Natural Step and Corporate Knights. (2021, November). *Canadian Pensions Dashboard for Responsible Investing: A Navigational Tool to Increase Ambition for a Sustainable, Inclusive Future*. institute.smartprosperity.ca/sites/default/files/Pensions-Dashboard.pdf.

2 Smart Prosperity Institute and Global Risk Institute. (2022, July). *Building Climate Resilience in Canada's Pension Funds.* institute.smartprosperity.ca/sites/default/files/Building%20Climate%20Resilience%20in%20Canada%E2%80%99s%20Pension%20Funds.pdf.