Our climate-related financial disclosure 2023/24

Contents

In 2022/23 we included the TCFD report within our Annual Report and Accounts. As TCFD reporting evolves and improves, we have decided to revert to issuing a stand-alone report. This is to ensure limited space in the Annual Report does not prevent proper disclosure.

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Chapter 1

Executive Summary

1.1 As a regulator, the FCA has limited exposure to climate-related financial risks. There is some risk to cash flow arising out of transition and physical risks. We do face regulatory challenges from climate-related risks in the firms we regulate.

1.2 Our view is that there are 2 climate-related financial risks to FCA cash flow:

a. Severe damage to FCA premises or a systems outage due to extreme climate events causing interruption to cash inflows and additional unbudgeted costs.
b. Major disruption to financial markets due to climate-related losses (eg a crisis in the general insurance market due to storms, floods or other physical events). These could require us to suddenly find additional regulatory resource to respond appropriately. This additional resource is likely to increase costs in the short term which might have a material effect on cashflow at an organisation level.

1.3 Our view is that in the short to medium term (up to 5 years) there is a low probability of a material effect on cash flow because:

a. Our business continuity plans should be sufficiently robust to firstly, enable a work from home model if we suffer the long-term loss of premises and secondly, to recover data and systems availability within costed business continuity plans
b. Based on the experience of the Covid pandemic, we should be able to shut down lower priority work and rapidly move resource to meet the demands of a sudden and unexpected crisis without the need to hire additional staff

Chapter 2

Introduction

2.1 We are committed to strengthening our environmental performance, including on climate issues. We are also mindful of the new regulatory principle introduced by the Financial Services & Markets Act 2023, for the FCA to have regard to '*the need to contribute towards achieving compliance by the Secretary of State with section 1 of the Climate Change Act 2008 (UK net zero emissions target)) where* [the FCA] *considers the exercise of its functions to be relevant to the making of such a contribution*.'

2.2 We have undertaken to achieve net-zero emissions as an organisation by 2045. As regards the markets we regulate, we are committed to support a market-led transition to a net zero, sustainable future.

How the TCFD applies to the FCA

2.3 We have undertaken to produce a TCFD report on a voluntary basis. As a public body established as a company limited by guarantee, we do not have shareholders or raise capital. We do not raise finance in the conventional manner and do not hold financial assets, apart from cash. However, we do need to manage our cash flow. So we must consider whether climate-related financial losses might destabilise financial market sectors or cause physical damage to our infrastructure, causing unexpected and unbudgeted costs and pressure on our cash flow.

2.4 The Greenhouse Gas (GHG) protocol identifies 15 categories of scope 3 emissions, the 15th of which is Investments. As a result, financial firms often include financed and facilitated emissions associated with investment and lending as a part of their scope 3 emissions. As authorising and supervising regulated firms cannot be viewed as investing in or lending to these firms, this falls outside the scope of Category 15. We are not therefore proposing to report such emissions as a part of our scope 3 emissions. We are reporting on other GHG scope 3 categories as appropriate.

2.5 We will be reporting on risks to both our own operations and our regulatory functions. These disclosures will be separate where appropriate.

2.6 In our work on transparency on climate-related risks and opportunities, we are clear that organisations should start to disclose climate risks and opportunities even when there are gaps in data and techniques. We have committed to producing an annual climate-related financial disclosure and expect future iterations to build on our previous experience to strengthen our metrics and methodologies.

Chapter 3

Governance

a) Describe the board's oversight of climate-related risks and opportunities

3.1 The FCA's Board sets the organisation's strategic direction and promotes its long-term success. It leads the organisation within a framework of prudent and effective controls that best support the assessment and management of risk, including climate-related risks (see Risk Management below).

3.2 We are required by section 3C of the Financial Services and Markets Act 2000 (as amended) to have regard to generally accepted principles of good corporate governance. The Board seeks to comply with the principles of the UK Corporate Governance Code as far as appropriate. We are now applying cross-FCA governance and our Risk Management Framework to identifying and managing climate-related risks across everything we do.

3.3 We are accountable to Parliament, including the Treasury Select Committee (TSC) and the Public Accounts Committee (PAC).

3.4 The Board has established committees to which it has delegated specific powers, duties and decision-making. These include the Audit, Risk and Nominations Committees. Each of these committees has responsibility for oversight of some aspect of the organisation's approach to managing climate-related risks and opportunities. For instance:

3.5 The Risk Committee provides assurance to the Board on the effectiveness of the organisation's system of risk management and regulation, to ensure that the FCA achieves its statutory and operational objectives. The committee reviews the adequacy of the FCA's Risk Management Framework and processes, including "*the need to contribute towards achieving compliance by the Secretary of State with section 1 of the Climate Change Act 2008 (UK net zero emissions target)* .... where [the FCA] *considers the exercise of its functions to be relevant to the making of such a contribution*" [Section 3B of FSMA 2000]

3.6 The Audit Committee monitors the integrity of the organisation's financial statements and oversees the consideration of any material climate-related risks when developing its financial statements. It also ensures environmental risks are considered as part of the organisation's governance and control framework.

3.7 The Nominations Committee makes recommendations to the Board on maintaining an appropriate balance of skills on the FCA Board and its committees. The committee also sets performance objectives for the Chief Executive and those within the scope of the Senior Managers Regime, which may incorporate climate-related expectations, measures and targets.

3.8 The Board considers climate-related issues and metrics annually as a minimum, as part of its review of the FCA's Business Plan, Annual Report and annual climate-related financial disclosure.

3.9 We have established an ESG Advisory Committee to support the FCA in executing oversight of relevant ESG-related issues both as a corporate entity and as a regulator. Chaired by the Director of ESG, the membership comprises 6 independent external experts, with a standing invitation to non-executive Board members (including the Chair). The Committee's role is advisory, therefore it is not a decision-making body.

b) Describe management's role in assessing and managing climate-related risks and opportunities

Our executive committees' roles with respect to climate issues

3.10 Our executive-level committees play an integral role in our governance.

3.11 Our Executive Committee (ExCo) oversees our general strategy and activities at the direction of the Board. This includes delivery of the FCA's Business Plan, which sets out the key activities we are undertaking in 2024 on climate change, in line with our ESG strategy and broader FCA Strategy.

3.12 ExCo also has overarching responsibility for our operational risk management. Related to this, the committee agrees our business continuity planning and is responsible for crisis management, in line with our Crisis Planning and Response Framework. These cover any risks to our operations, including those arising from climate events (eg flooding and other physical risks to property).

3.13 The Executive Regulation & Policy Committee (ERPC) is responsible for executive decision-making on policy decisions and regulatory issues. Roles it undertakes on climate issues include:

- providing direction on the overall outline and approach to strategic and major policy initiatives, including those involving climate change and other ESG matters.
- reviewing and challenging regulatory risks to our objectives and ensuring all elements of identifying and mitigating regulatory risk across the FCA are joined up and effective.
- deciding, approving, reviewing or challenging any issue referred to it in line with the executive procedures, including regulatory decisions.

3.14 Executive accountability

3.15 The CEO has ultimate responsibility for implementing the FCA strategy agreed by the Board. This includes the ESG-related commitment within the FCA Strategy. The CEO may delegate authority to one or more Executive Committees, per the structure above. The CEO may also delegate to one or more individuals (eg the Chief Operating Officer for our own operations).

3.16 Our Director of ESG reports directly to the CEO with a mandate to embed climate and wider ESG considerations across the FCA's functions (a 'golden thread' approach). This is covered in the objectives against which the CEO assesses the ESG Director's performance. The ESG Director is a member of ERPC, ensuring that climate and sustainability-related issues are factored into regulatory and policy discussions and decision making.

3.17 Role of management below executive level

3.18 We have a range of structures to help our management consider and address climate risks and opportunities below the level of our executive and its committees. These include:

- Our ongoing work to embed climate considerations into our supervisory and authorisations processes, across everything we do.
- Divisional Risk Committees and Operations Committees, which consider (among other things) climate-related projects and initiatives in their areas.
- A dedicated ESG market intelligence team, which collaborates with other intelligence gathering teams across the FCA.
- The regular management operations of the ESG Division and Operations Division, including their leadership meetings where climate-related considerations are discussed as required.
- The regular management information from Operations Division on our environmental and sustainability performance (eg data on our GHG emissions, including our key suppliers). This is an important part of the reporting to enable our ESG Director to oversee our performance against environmental and sustainability targets.

3.19 Our Corporate Governance Statement gives more details.

Chapter 4

Strategy

4.1 Our 'golden thread' approach to embedding ESG considerations helps ensure our activities:

- contribute to the Government's commitment to achieving a net zero economy by 2050
- seek to reduce climate-related (and broader sustainability) risks to consumers, firms and markets
- support a market-led transition by the financial services industry to a net zero, sustainable future

4.2 Our work on sustainable finance advances our primary objectives of consumer protection, market integrity and competition in the interests of consumers and our secondary competitiveness and growth objective.

4.3 We also consider the promotion of sustainable growth in the UK economy in the medium or long term and must 'have regard', where relevant to our functions, to the need to contribute towards the Government achieving compliance with:

- the net zero emissions target
- environmental targets

4.4 In practice, this means we focus on engaging and collaborating with industry to deliver a framework that will build and consolidate the UK's sustainable finance leadership and to ensure the UK is a trusted and stable environment for consumers but also for firms to compete, grow and innovate.

4.5 We also actively promote international alignment of standards for climate-related financial disclosure. For example, contributing to the work of the International Sustainability Standards Board.

4.6 This chapter examines how the risks and opportunities arising from climate change have affected how we operate and our strategic approach. We differentiate between our regulatory functions and our own operations and consider the ramifications of different climate scenarios. We use scenario analysis to explore how different transition pathways could affect the sectors we regulate and the cash flow implications for us.

a) Describe the climate-related risks and opportunities the organisation has identified over the short, medium, and long term

Our regulatory functions

4.7 Climate risks can be categorised broadly into physical risks and transition risks. Physical risks are caused by changes in climate and an increase in the frequency and severity of weather events. These can damage infrastructure, disrupt supply chains and worsen working conditions. Transition risks are caused by the adjustment towards a net zero economy, which may involve significant changes to policy, technology, law, and investor and consumer attitudes.

4.8 Physical and transition risks can further drive existing types of financial risks. While, for example, the drivers of Business Continuity Risk, Health and Safety Risk, and IT Systems Availability and Resilience Risk are not limited to environmental factors, climate change can potentially worsen or trigger these risks and events. These may translate into harms for consumers and markets. From a regulatory perspective, this poses threats to our operational objectives of protecting consumers, protecting financial markets and promoting competition in the interests of consumers. The FCA may face unanticipated costs in dealing with such harms which may affect cash flow.

4.9 With the Prudential Regulation Authority (PRA), we co-chair the Climate Financial Risk Forum (CFRF) of industry representatives and other stakeholders. The CFRF's purpose is to build capacity and share best practice to advance the financial sector's responses to the financial risks from climate change. Since the CFRF's establishment in 2019 we have invested significant resource into convening and facilitating the CFRF's work programme across topics including disclosures, risk management, innovation and scenario analysis.

4.10 In June 2020, the CFRF published a guide to help firms manage and adapt to climate-related risks and opportunities. This set out how physical risks and transition risks can be reflected in:

- insurance underwriting risk
- credit risk
- financial market risk
- operational risk

4.11 We discussed each of these risks, and the additional risks of asset write-downs and reputational impacts, in the Climate Change Adaptation Report (CCAR) we published in October 2021 (see Chapter 4 of the CCAR). We also identified that ESG data gaps might affect firms' ability to address these risks. And we set out an initial overview of how climate-related transitional and physical risks and harms were reflected in the following sectors:

- pensions and retirement income
- retail investments

- retail lending
- wholesale markets
- general insurance underwriting

4.12 The risks are broad in nature and affect a range of different firms and are relevant over the short, medium and long terms. For instance, climate-related insurance underwriting risks may crystallise in any given year (eg from flooding, snowfall or wildfires). Or they may affect the business model and future prospects of a firm over the medium or long terms, requiring a wholesale review of strategy.

How climate-related risks and opportunities affect regulated financial sectors

4.13 Building on our CCAR analysis, this section summarises the climate-related risks and opportunities across each of these sectors, including relevant risks of harm to consumers and markets.

a) Financial institution operations

4.14 The main climate risks for most financial institutions are the impact of physical and transition risks on their counterparties and the assets they hold or manage, as well as insurance underwriting.

4.15 Concentrations of lending, investing, trading and underwriting for carbon-intensive sectors such as oil and gas, manufacturing, transportation and construction create the most material exposures for financial market participants.

4.16 However, financial firms with physical operations such as offices, data centres and branch networks could also be exposed to physical risks from their own operations. We expect firms to take these risks into account in how they operate and plan for the future.

b) The FCA's own operations

4.17 We are committed to achieve net-zero by 2045. There will inevitably be costs associated with transition, however we do not currently predict these will have a material effect on cash flow.

4.18 In this section we discuss the risks to our ability to carry out our regulatory and operational activities (which we term 'Own Risks'). Own risks have 2 elements: Operational Risks and Execution Risks. These risks arise from our organisation and operations, particularly those involving our internal processes, people and/or systems, including our IT and infrastructure. These risks are relevant across the short, medium and long terms and may become more likely/severe over time.

4.19 While the FCA alone cannot mitigate climate change, it is important we continue to make progress towards achieving net zero. We are following a programme of continual improvement in how we operate. This is targeted at driving environmental efficiency and the best use of our resources.

4.20 Our key objectives for the 2024/25 financial year are:

- committing to and validating emissions reductions in line with science-based targets
- improving internal awareness and action on environmental aspects of how we operate and adopting sustainable practices in our operations and approach to policy

4.21 We have developed an Environmental Management System that supports our aim of becoming a more sustainable organisation through:

- improving our environmental performance. This includes working collaboratively with staff and our suppliers, in line with our Environmental Policy Statement.
- complying with statutory obligations, such as national and local environmental regulations and statutory requirements for environmental performance reporting.
- maintaining our certification, ISO14001:2015 'Environmental Management System for Financial Regulation', supported by a programme of continual improvement.

b) Describe the impact of climate-related risks and opportunities on the organization's businesses, strategy, and financial planning

4.22 Since the 2019/20 financial year, climate change and sustainable finance has been a one of the FCA's priorities.

4.23 As a result, we established an ESG division in 2021 to better respond to sustainability challenges, including climate change. The ESG division is responsible for the FCA ESG strategy.

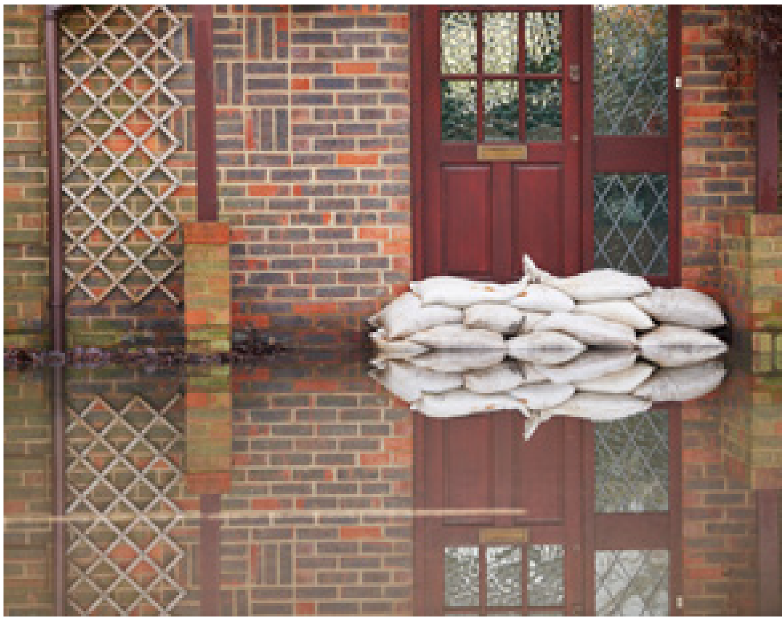
4.24 In terms of financial planning, the physical risks to our own operations form part of our wider business continuity planning.

c) Describe the resilience of the organization's strategy, taking into consideration different climate-related scenarios, including a 2°C or lower scenario

4.25 We consider 3 Network for Greening the Financial System (NGFS) scenarios and the impact they may have on 5 key financial services sectors - retail lending, pensions and retirement income, retail investments, wholesale markets and general insurance - and therefore the resilience of our regulatory function.

4.26 We then consider the impact of these 3 scenarios on our own operations and the resilience of our business continuity planning.

4.27 The 3 scenarios are:



NGFS Net-Zero 2050 scenario

4.28 An ambitious scenario that limits global warming to 1.5 °C through stringent climate policies and innovation, reaching net zero CO_2 emissions around 2050. Some jurisdictions such as the UK, US, EU and Japan reach net zero for all greenhouse gases by this point.

NGFS Nationally determined contributions (NDCs) scenario

4.29 Includes all pledged policies even if not yet implemented. This scenario assumes that the moderate and heterogeneous climate ambition reflected in the conditional NDCs at the beginning of 2021 continues over the 21st century. Even assuming pledges are actually implemented, emissions decline but lead nonetheless to 2.6 °C of global warming creating moderate to severe physical risks. Transition risks are relatively low.

NGFS Fragmented world scenario

4.30 Scenario assumes delayed and divergent climate policy ambition globally, leading to elevated transition risks in some countries and high physical risks everywhere due to the transition's overall ineffectiveness. Countries without net zero targets follow current policies, while other countries (including the UK) achieve theirs partially (80% of the target). 3 °C plus of warming can be expected by 2050.

4.31 It is important to note that changes to mean UK temperature and precipitation is likely to differ from changes to global mean temperature and precipitation.

4.32 The following diagram shows the level of transition and physical risks for each scenario:

Figure 1

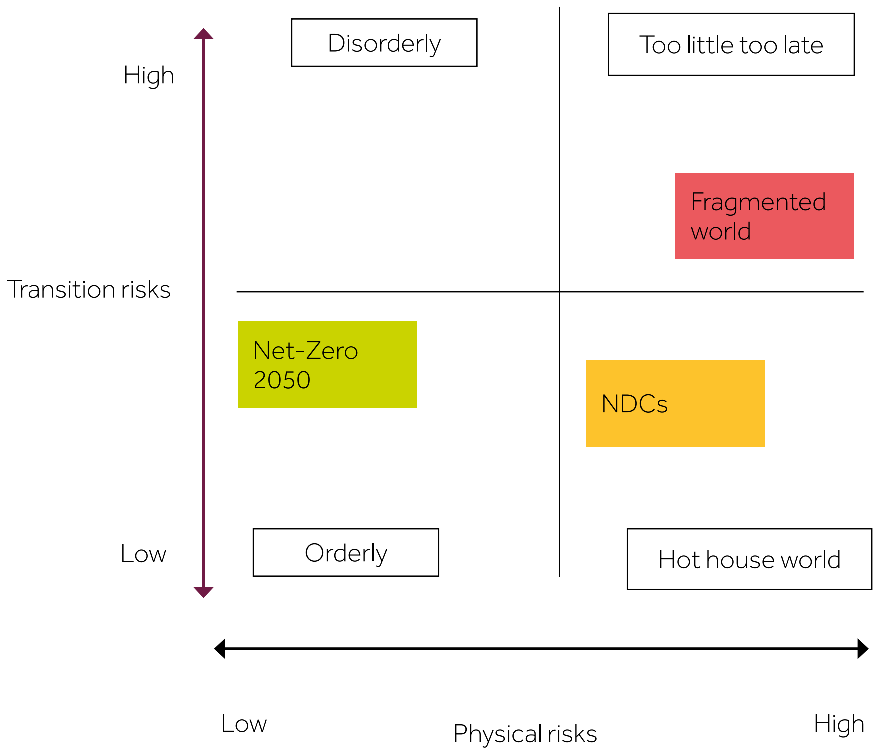
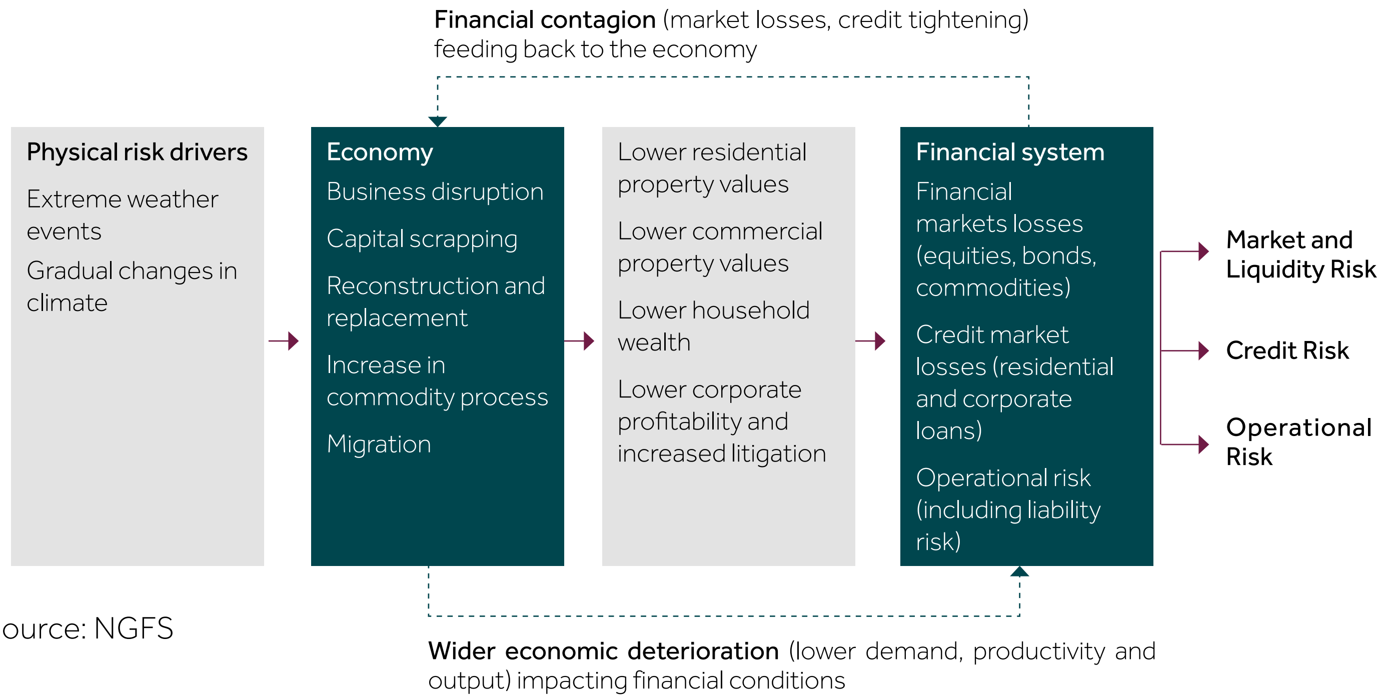


Figure 2: From physical risk to financial stability risks



Source: NGFS

4.33 Physical risks can be expected under all 3, the difference being the frequency and severity of these risks and hence the financial impacts. The economic effects are mapped in the diagram above.

Chapter 5

Risks affecting our regulatory function

NGFS Net zero 2050 scenario

Sector	Transition Risks	Physical Risks
Retail Lending	Significant legal, regulatory and operational costs driven by robust climate policies.	The risk of property damage impairing loan collateral, which may lead to losses on bank lending. This could result in consumers being unable to re-mortgage and 'trapped' on the current lenders standard variable rate.
Pensions & Retirement Income	Significant legal, regulatory and operational costs driven by robust climate policies. Write-downs due to transition risks could lead to reduced consumer confidence or greater firm or consumer risk-taking to compensate.	Some risk of investment underperformance driven by the physical risks associated with 1.5°C. For example, damage to property and consequent business interruption or a slowdown in economic activity during extreme heat waves.
Retail Investments	Significant legal, regulatory and operational costs driven by robust climate policies. Write-downs due to transition risks could lead to reduced consumer confidence or greater firm or consumer risk-taking to compensate.	Some risk of investment underperformance driven by the physical risks associated with 1.5°C.
Wholesale Markets	Significant legal, regulatory and operational costs driven by robust climate policies. Stranded assets/impaired collateral due to investment in/lending to high carbon industries.	Increased risk of property damage may impair collateral leading to losses on bank lending.
General Insurance Underwriting	Significant legal, regulatory and operational costs driven by robust climate policies. Possible initial increased underwriting costs as insurers price coverage of new technologies. Possible increase in Directors & Officers claims by shareholders driven by Board inaction on climate, leading to financial losses.	Increased frequency and/or severity of storms, rainfall and extreme heat events lead to increased property damage claims. Flooding, wind damage, accelerated coastal erosion, subsidence and wildfires all contribute. General increases in premiums may cause affordability problems for consumers. Localised unavailability of cover possible. Insurers capital may be eroded.

NGFS Nationally determined contributions (NDCs) scenario

Sector	Transition Risks	Physical Risks
Retail Lending	Some legal, regulatory and operational costs.	Increased risk of property damage may impair collateral leading to losses on bank lending, particularly when combined with unavailability of insurance coverage. Increased numbers of consumers unable to re-mortgage.
Pensions & Retirement Income	Some legal, regulatory and operational costs. Slower rate of transition may still lead to some write-downs and could lead to some loss of consumer confidence or greater firm or consumer risk-taking to compensate.	Broad underperformance due to climate-related losses driven by the physical risks associated with 2.6°C of global warming.
Retail Investments	Some legal, regulatory and operational costs. Slower rate of transition may still lead to some write-downs and some loss of consumer confidence or greater firm or consumer risk-taking to compensate remains possible.	Broad underperformance due to climate-related losses driven by the physical risks associated with 2.6°C of global warming.
Wholesale Markets	Some legal, regulatory and operational costs. Given partial transition, some risk of stranded assets/impaired collateral due to investment in/lending to high carbon industries.	Broad underperformance due to climate-related losses. Increased risk of property damage may impair collateral, leading to losses on bank lending, particularly when combined with unavailability of insurance coverage.
General Insurance Underwriting	Some legal, regulatory and operational costs. Increased underwriting costs as insurers price coverage of new technologies remains a risk. The possible increase in D & O claims by shareholders driven by Board inaction on climate becomes more likely.	Significantly increased frequency and/or severity of storms, rainfall, accelerated coastal erosion, sea-level rises, subsidence and extreme heat events lead to greatly increased property damage claims. Cover for such events may become unavailable for many consumers. Some insurers may fail or withdraw from some parts of the market, especially if reinsurance is withdrawn or becomes unaffordable.

NGFS Fragmented world scenario

Sector	Transition Risks	Physical Risks
Retail Lending	Some legal, regulatory and operational costs.	Increased risk of property damage becomes increasingly likely to impair collateral leading to losses on bank lending, particularly when combined with the increased risk of unavailability of insurance coverage. Increased numbers of consumers unable to re-mortgage.
Pensions & Retirement Income	Some legal, regulatory and operational costs. Even an insufficient rate of transition could still lead to some write-downs although less likely to lead to material financial losses.	Higher morbidity driven by higher temperatures may increase asset outflows and reduce inflows as consumers access savings sooner. Higher mortality may likewise see increased asset outflows, only partially offset by reductions in annuity liabilities. Significant risk of asset write downs following physical weather events.
Retail Investments	Some legal, regulatory and operational costs given partial transition. Write-downs cannot be ruled out.	Significant risk of asset write- downs following physical weather events. Investment underperformance due to increased likelihood of climate-related losses and associated economic impacts.
Wholesale Markets	Some legal, regulatory and operational costs. Given partial transition, some risk of stranded assets/impaired collateral remains due to investment in/lending to high carbon industries.	Broad underperformance due to climate-related losses. Increased risk of property damage may impair collateral (for example mortgage-backed securities) leading to losses on bank lending, particularly when combined with unavailability of insurance coverage.
General Insurance Underwriting	Some legal, regulatory and operational costs given partial transition.	Very significantly increased frequency and/or severity of storms, rainfall, accelerated coastal erosion, sea-level rises, subsidence and extreme heat events lead to greatly increased property damage claims. Reinsurance likely to become unavailable for many property risks and the failure of reinsurers is possible, which is likely to cause the failure of some of the insurers they cover. Many insurers may withdraw from the market or even fail, particularly if not reinsured. Cover for such events likely to become unavailable for many consumers.

Conclusion

5.1 The risk to our regulatory function would be the costs of managing a climate-driven crisis in a regulated market.

5.2 While some effects of climate change are already being seen, under the Net Zero 2050 scenario and in the short term under all scenarios, we consider that we could manage the impact by re-deploying existing resource from non-essential work.

5.3 In the longer term, under the NDC or Fragmented World scenarios, this becomes less certain. The interconnectivity between market sectors could lead to a crisis in one sector causing issues in other sectors. This might prevent or limit re-deployment of resource.

Risks affecting our own operations

5.4 **Net zero 2050 scenario** – We have a robust and comprehensive transition plan for our operations, underpinned by a clear net zero commitment and associated near-term targets. We will continue to strengthen our understanding of our own Scope 3 GHG emissions data and integrate this into how we engage and select our suppliers. In future, we may also need to consider the financial impact of transition risks relating to policy change into our operational costs. For example, because of a carbon tax or requirements for the energy fuel mix in power generation.

5.5 **Nationally determined contributions (NDCs) scenario** – Current UK policy pledges would not be enough to achieve net-zero by 2050. Given this, while expected transition risks might be reduced, physical risks would increase. As a result, the FCA could face business continuity disruptions from a significant increase in heatwaves, flooding and power outages. Such extreme weather events could disrupt staff's ability to work both in the office and at home. We would therefore need to continue to invest in ensuring all of our activities, and those of our core suppliers, service providers and data centres, can be carried out remotely where needed.

5.6 **Fragmented world scenario** – Transition risks would still remain despite the failure to fully implement policy pledges (NDCs), perhaps only slightly lessened. Increased frequency and severity of extreme weather events over the NDC scenario would lead to greater business continuity risks.

Conclusion

5.7 We consider that our business continuity planning is sufficiently resilient to manage risks to our own operations under the net-zero 2050 scenario and in the short to medium term (3 to 5 years) under the other scenarios. In the longer term it becomes more difficult to judge resilience, particularly under the Fragmented World scenario.

5.8 We are committed to achieve net-zero by 2045 and our transition risks would be similar under all 3 scenarios.

Risk management, metrics and targets

a) Describe the organisation's processes for identifying and assessing climate-related risks

5.9 Achieving our statutory and operational objectives relies on our ability to influence the conduct and culture of the industry we regulate and our own ability to operate effectively. It also relies on the financial resilience of firms to the risks they face, which is important to us as the prudential regulator of 45,000 firms.

5.10 Our risk management framework is designed to help us make regulatory judgements about the risks of harm, including climate-related risks, and how we should prioritise our interventions, including through analysing trends and identifying emerging risks.

5.11 Climate risks could affect our ability to achieve our objectives, and hence directly influence our work as both a regulator and a corporate entity. We will take the necessary steps to manage these risks effectively, and to further develop how we measure our impact. This in turn should further improve our ability to mitigate associated consumer and market harms.

5.12 To identify, assess, track and mitigate risks, our risk management framework includes an organisation-wide operating model built around the three lines of defence:

- First line: Our front-line operations identify, assess, mitigate, and report consumer and market harms, as well as manage Own Risks.
- Second line: Our Risk & Compliance Oversight Division (R&CO) owns the Risk Management Framework for our Own Risks and provides risk management expertise, advice, support, challenge and oversight. It also provides independent assurance of overall risk management processes.
- Third line: Our Internal Audit function provides independent challenge to the standards and effectiveness of risk management across the organisation.

5.13 This gives us a robust approach to directly manage and control our Own Risks, namely the risks to our operations and how we execute our regulatory strategy. This in turn helps to ensure we effectively identify, assess, mitigate, manage, and report risks of harm to consumers and markets, as well as any associated public confidence risks.

5.14 As noted previously, the Board has amended the Terms of Reference of key board committees to refer to reviewing and challenging key climate risks and any mitigating actions we have taken. This includes the Risk Committee and Audit Committee.

b) Describe the organisation's processes for managing climate-related risks

5.15 Our risk taxonomies enable us to categorise risks consistently to help improve the adequacy, effectiveness and efficiency of our risk management activities. We use 3 different risk categories that cover:

- Risk of Harm – risks posed to consumers, firms and markets
- Cause of Harm – factors which can lead to harm if not addressed
- Own Risk – operational and execution risks facing us as an organisation

5.16 To embed climate risks into our risk management framework, we have ensured that our risk taxonomies support the categorisation and tracking of ESG risks. This provides a clear and consistent tool for staff across the FCA to identify and categorise climate-related risks. Our Risk of Harm and Cause of Harm taxonomies enable us to map climate-related risks that could affect the markets we regulate and their consumers. Likewise, we have mapped the climate-related risks that could affect our ability to operate and carry out our functions to our Own Risk taxonomy.

5.17 One or more or members of our senior management team also have responsibility for relevant elements of the Own Risk taxonomy in line with their overall responsibilities.

Risk identification and assessment

5.18 We have sought to assess, develop and enhance our Own Risk management capabilities within the ESG Division, using existing organisational risk management strengths and existing best practice. For example, implementing science-based targets for our planned emission reductions.

5.19 This should in turn help us ensure we effectively identify, assess, mitigate, manage, and report on external ESG-related Risks of Harm, and that we are better able to deliver the right interventions at the right time and in the right way.

5.20 We have a range of mechanisms to identify risks and their causes in practice, including those related to climate. In terms of our regulatory role, these range from the work of our supervisory and Market Oversight teams via their direct interactions with financial firms/sectors and listed companies, to the role of our ESG Division and other areas in gathering intelligence and data on external developments. For instance, our Financial Lives Survey (FLS) is a major source of information on consumer trends and risks.

5.21 The FLS now includes ESG-related questions to assess consumers' interest in, and engagement with, ESG and responsible investing, including climate-related investing. There are also questions about assessing greenwashing risks, where products promoted as being 'sustainable' overstate or mislead about their actual ESG-credentials.

5.22 We have a range of mechanisms to identify risks and their causes in practice, including those related to climate. We will be using the FLS, and other means of gathering consumer and firm insight, to identify and assess a wider range of climate-related risks that may affect consumers. Our risk identification is augmented by the ESG Advisory Committee, who provide independent challenge and guidance.

5.23 We have a dedicated Intelligence team within the ESG Division to improve our ability to identify climate-related risks. We also have an ESG Advisory team working with other FCA sectors to help in identifying and recording sustainability-related risks. We summarise below the steps we have taken to embed climate considerations in how we regulate. Our international presence, for example on IOSCO's Sustainability Task Force, provides us with a global perspective on sustainability risks.

c) Describe how processes for identifying, assessing, and managing climate-related risks are integrated into the organisation's overall risk management

5.24 We have central risk management systems in place to store, manage, aggregate and report on the risks we identify. This helps to ensure that risks are identified, categorised, assessed consistently, tracked and managed. It also helps us to have effective reporting and governance in place, all of which improves our ability to provide joined-up, effective interventions at the right time.

5.25 Oversight of the risks and objectives as they affect how we operate is provided by members of our senior management team or by ExCo, as set out in the Governance section of this report. This oversight includes reviewing and approving our assessment and management of operational risk, for example the risk of climate events affecting our ability to discharge our functions. It also includes reviewing and signing off the environmental objectives, targets and metrics that we set as an organisation, eg to reduce our GHG emissions.

Risk tolerance

5.26 Once we have used our risk taxonomies and wider tools to understand the risks we face, we can decide whether and how to act. Our risk appetite framework incorporates specific key risk indicators of climate-related risks from our own operations. Our Annual Report covers how we develop key risk indicators for our regulatory activity, where we also discuss progress towards our ESG priority.

5.27 Our approach to measuring, mitigating, and managing climate risks will continue to evolve as our understanding of the risks grows, methodologies improve and we strengthen our own technical capabilities.

Risk evaluation

5.28 The final aspect of our approach to risk management is evaluation. We evaluate the differences between the actual and intended outcomes of our actions and identify where we can improve our approach. We continue to strengthen our approach to evaluating our own impact as an organisation, including in terms of climate change.

5.29 The climate-related metrics and targets we discuss below, relating to our own environmental performance, help us to do this in a robust and transparent way. Our ESG Division will lead the annual evaluation and disclosure of how we have performed against our set outcomes and managed the associated risks. This will then be challenged through our organisational governance.

5.30 Further steps we have taken to embed climate considerations in our risk approach

5.31 As well as the above, we have taken a number of further steps to embed climate considerations in our approach to risk:

- We have introduced an anti-greenwashing rule applying to all authorised firms who make sustainability-related claims about financial products and services, together with more specific rules about the naming and marketing of certain investment products.
- Enhancing our broader processes. We have also integrated ESG considerations into supervisory and policy committees, forums and processes dealing with climate risks, including through experts attending relevant committees. This helps to ensure we understand and factor in climate considerations when we make supervisory and policy decisions.
- Providing colleagues with the training and tools they need. This has included ensuring they are aware of climate issues, how they relate to our statutory and operational objectives and what questions they should be asking regulated firms and individuals to assess climate risks (including how to recognise good versus poor responses).
- Reviewing the climate-related requirements for suppliers, based on underlying risk, and ensuring that we improve our procurement processes to get assurance these requirements are met.
- Liaising with other regulators, such as the PRA, on emerging and existing climate-related risks and how we can work together to address them. These changes are materially improving our capacity to identify, assess and mitigate climate-related risks.

Chapter 6

Metrics and targets to evaluate our response to climate-related risks and opportunities

6.1 As outlined in our Strategy and Business Plan, as well as our ESG Strategy, we are committed to being accountable, through clear outcomes, metrics and targets, including for our ESG priorities. This section outlines the climate-related metrics and targets we use across both our internal operations and regulatory activity.

a. Disclose the metrics used by the organisation to assess climate-related risks and opportunities in line with its strategy and risk management process

Metrics and targets for our regulatory activity

6.2 In our ESG Strategy, we outlined our cross-cutting commitment on ESG. As a part of this strategy, we undertook to develop metrics and targets for our regulatory work. This has proved challenging due to costs and data availability. We know we still have work to do in this area.

6.3 In improving trust and consumer protection, we faced further challenges due to the difficulty in defining misleading sustainability-related marketing (greenwashing). We have introduced an anti-greenwashing rule applying to the products and services of all authorised financial services sectors. This came into effect on 31 May 2024. More specific rules on the naming and marketing of certain investment products have been introduced and are scheduled to come into effect on 2 December 2024. We believe this will significantly help us identify and act against greenwashing.

6.4 We published the metrics we wanted to put in place to assess our success against the outcomes we want to achieve. All the metrics are relevant to climate-related risks and opportunities and are summarised below. We introduced these metrics for the 2022/23 financial year. As we did not have baselines against which to judge them, we did not set specific, numeric targets. We are revisiting outcomes, targets and metrics as our work on ESG issues progresses, to continuously improve.

Metrics and targets for our regulatory activity

6.5 We have published our climate-related metrics for our regulatory activities.

Metrics and targets for our own operations

6.6 Metrics and targets to manage our own operational climate-related risks and opportunities and our performance against them can be found in our Environmental Sustainability Report and in our net zero transition plan.

b. Disclose Scope 1, Scope 2, and, if appropriate, Scope 3 greenhouse gas (GHG) emissions, and the related risks

6.7 Our Environmental Sustainability Report, gives our metrics and targets to manage our own operational climate-related risks and opportunities, and our performance against them, including our GHG emissions.

c. Describe the targets used by the organisation to manage climate-related risks and opportunities and performance against targets

6.8 We do not currently have any targets for climate-related risks from our regulatory activities.

6.9 As regards our own operations, our Environmental Sustainability Report shows our targets.

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