

Written evidence submitted by UK Finance

About UK Finance

1. UK Finance is the collective voice for the banking and finance industry. Representing around 300 firms across the industry, we act to enhance competitiveness, support customers and facilitate innovation.

Summary

2. We welcome the opportunity to provide evidence to the Environmental Audit Committee's inquiry into the financial sector and the UK's net zero transition. We are committed to the transition and are a supporting institution of the Net Zero Banking Alliance (NZBA). Many of our members are also members of the Glasgow Financial Alliance for Net Zero through their membership of the NZBA. We agree with the Committee that the banking and finance industry, as part of the broader financial services sector, must play a critical role in achieving net zero. However, this requires an enabling policy environment, facilitated by bold government leadership, to support the urgent, whole-economy transition. In particular:
 - the UK Government and devolved governments (hereafter "the UK's governments") should provide robust, coherent, sector-by-sector policy on the path to net zero, especially with relation to greening the housing stock. This will allow the whole economy, including the banking and finance industry, to better align with the UK's sustainability goals; and
 - the UK's governments should continue to play an active role in requiring and enforcing disclosure of sustainability-related risks and impacts and in advocating for and securing increased coherence of disclosure and risk management approaches internationally. Reliable data are an important component of assessing banking and finance firms' sustainability impacts and fully integrating them into decision making.
3. If you have any questions relating to this response, please contact Ian Bhullar, Strategic and Sustainability Policy Principal.

Robust UK net zero policies

4. The banking and finance industry is developing and implementing its green finance obligations and ambitions at pace, for example by setting out ambitious transition plans and deploying innovative products. However, alignment with the UK's sustainability goals can only happen as part of a whole-of-economy transition, recognising that firms' balance sheets – and particularly those of systemically important banks – are a reflection of the wider economy.
5. To enable this, the UK's governments must provide a robust, clear and coherent policy framework for the real economy, sector by sector, to achieve net zero. In a wide variety of sectors, the net zero and wider sustainability policy trajectory remains vague, without clear milestones leading to full decarbonisation and therefore sufficient certainty about which winners to back.

6. The banking and finance industry alone cannot be responsible for fixing this absence of clarity as it often lacks real-world opportunities in which to invest, while policy ambiguity can make it difficult for firms to provide clear advice to clients because of the conduct risks it raises. The UK's governments need to use the policy and fiscal levers at their disposal to address key market failures. This should include:
 - roadmaps for key emitting sectors, setting out interim milestones for achieving goals, and clarity on technological choices where appropriate (e.g. heat pumps vs hydrogen);
 - targeted use of public financing to crowd in private finance and/or drive down the costs of new technologies, drawing on existing processes and institutions (e.g. the UK Infrastructure Bank, the British Business Bank and the Scottish National Investment Bank);
 - targeted policy interventions that help address specific barriers, for example the skills deficit in some new/rapidly growing sectors; and
 - greater support for SMEs and retail customers in understanding the impacts of the transition on their operations and/or finances. This will help create greater demand for green finance products, which in turn will facilitate the transition.
7. Responsible lending to carbon intensive sectors is a necessary part of the transition. As society collectively seeks to transition away from fossil fuels, those activities that are most polluting need finance to establish new, cleaner business models. The banking and finance industry faces serious reputational risks in supporting transition activities, for instance while financing polluting or high carbon industries and sectors to sharply reduce their emissions. Such industries are a widely recognised part of the transition, including by the Intergovernmental Panel on Climate Change and the International Energy Agency.
8. Lenders and real economy actors need to receive clear policy and guidance on acceptable investments and the acceptable trajectory in the context of transition activities. Public communications and campaigns should also raise awareness of the reality of the transition to net zero, to promote a reduction in energy demands and help mitigate reputational risks.
9. In sum, the green transition requires urgent, whole-economy, coordinated effort by government, the financial services sector and the real economy. We welcome closer collaboration with the UK's governments and industries to enable that change.

The regulatory environment, data and standardisation

10. Since the UK government published its first Green Finance Strategy in July 2019,¹ its deployment of sustainability disclosure requirements has helped improve data availability so that lenders are better able to integrate environmental-related factors into their decision-making. Access to client sustainability-related risk and impact data nevertheless remains a barrier to assessing banking and finance firms' Scope 3 emissions and therefore to fully integrating these factors into decision-making. Industry needs to collectively move toward standardised approaches for reporting in order to streamline and improve accuracy of analysis.
11. The UK government should continue to play an active role in requiring and enforcing disclosure of sustainability-related risks, impacts and transition plans by corporates as this remains critical to measuring the banking and finance industry's exposure across lending portfolios.
12. Domestically, the UK government and regulators can support this process by giving their backing to specific reporting methodologies, approaches and APIs (covering risks, impacts and transition plans) as well as by providing guidance on outstanding questions like the use of data proxies and estimates. Data should be easily imported and processed for use by banking and finance firms so that they can conduct actionable analysis across large lending books. Within transition plan reporting, HM Treasury's establishment of the Transition Plan Taskforce is a welcome step toward delivering clear guidance on how business models can be re-engineered.
13. There is also a need for specific guidance for SMEs, which make up a large portion of many banking and finance firms' Scope 3 emissions as either direct customers or components of supply chains. Access to SME sustainability data is particularly challenging. Similarly, improved access to energy performance data is desperately needed to allow firms to better measure their sustainability-related risks, for example via mortgage portfolios. This could be supported, for example, through real-time energy performance certification rating, buildings passports or real-time retail/actual energy use data.
14. Internationally, the UK government should continue to advocate for and secure increased coherence of disclosure and risk management approaches, including taxonomies, across jurisdictions. The increasing divergence of sustainability-related risk reporting and management expectations is a major burden on many firms, affecting those with multinational operations as well as those whose loan books or supply chains touch other countries. The UK government should continue to give its strong backing to the work of the International Financial Reporting Standards Foundation's International Sustainability Standards Board to build a single agreed baseline for reporting and to use other fora like the G20 and the G7 to encourage convergence on that baseline.

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¹ https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/820284/190716_BEIS_Green_Finance_Strategy_Accessible_Final.pdf.