

# Task Force on Climate-related Financial Disclosures 2023

**Building your future**

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# Introduction



**Society demands greater climate action. As a leading mutual building society, our commitment to achieving net zero and fostering climate awareness isn't just a box to tick – it's embedded in our social purpose. Through our Better Homes, Secure Futures, and Fairer Society ambitions, we're not only signalling our dedication to a sustainable future, but actively shaping it.**

This report not only highlights our commitment to transparent and responsible reporting, it also underscores our dedication to integrating climate risk awareness into our day-to-day business activities and overall strategy, as well as into our corporate governance and risk management activities.

We're being clear and consistent about our commitments, the progress we're making and the areas where we need to improve. Progress, however, isn't measured by intentions or words – it's quantified by action.

We've set both short and long-term carbon reduction targets, benchmarked against our own commitments as well as societal expectations. Our progress isn't abstract – it's tangible, measurable, and grounded in real outcomes. This year, we've enhanced our data collection processes to provide more comprehensive emissions reporting, shedding light on our energy usage and the efficacy of our initiatives in reducing our environmental footprint.

We know big challenges lie ahead. While Principality may not be a major carbon emitter, our responsibility transcends our own footprint. We aspire to be more than just a sustainable business – we want to champion sustainable practices in every way we can, not only to set a standard for our peers and to partner with suppliers who share our ambitions, but also to educate and empower our colleagues and customers to join us in the transition to a low-carbon lifestyle.

Tony Smith  
Chief Impact and Governance Officer



To comply with the Prudential Regulation Authority's Supervisory Statement 3/19 (SS3/19), intended to enhance banks' and insurers' approaches to managing the financial risks from climate change, we've obtained and analysed data relating to both the potential physical and transition risks arising from the portfolio of residential property mortgaged by the Society.

As our work evolves, and the impact of different scenarios is considered, we will assess financial risks by reference to our risk appetite and determine the most appropriate measures and targets to put in place. SS3/19 requires specific disclosures to be made regarding these risks, and these are included within this report.

Climate change considerations are embedded in the Society's governance model and future planning and, aligning to our Purpose, are intrinsic to how we operate. The Executive Committee and Board are fully engaged with our climate strategy, proposition development, risk management, and disclosures and have ultimate oversight of Principality's approach to considering, evaluating, and integrating climate-related risks and opportunities throughout the business on a day-to-day basis.

Recognising the importance of climate strategy to the business and our wider stakeholders, the Board approved the Society's Impact Strategy in November 2022. Underpinning our overall enterprise-wide strategy, elements within the Impact Strategy are focused on climate and sustainability-related initiatives and actions, aligning them with broader ESG considerations.

The Board Risk Committee (BRC) and Executive Risk Committee (ERC) are the key committees responsible

## Governance

for the oversight of the financial risks arising from climate change.

### Board Risk Committee

The Board has delegated oversight of climate risk management to the Board Risk Committee, although ultimate responsibility continues to reside with the Board. The Board Risk Committee receives regular updates on climate-related risk.

### Executive Risk Committee

ERC is chaired by the Chief Risk Officer (CRO), with membership formed from the Executive Committee. It has delegated authority from BRC to monitor and review the risk exposures in accordance with the Society's Enterprise Risk Management Framework (ERMF), Board risk appetite, and the Society's strategy and medium-term plan.

### Remuneration Committee

The Remuneration Committee had oversight of the review for senior management's remuneration for the financial year. Performance of the Society's Impact Strategy in relation to the Society's progress towards net-zero remains intrinsically linked to some of the targets and measures linked to remuneration. Further information on the responsibilities and oversight of the Remuneration Committee can be found in Principality's 2023 Annual Report and Accounts.

### Impact Working Group

This group was introduced in 2023 to provide oversight and monitor performance of the implementation of the Society's Impact Strategy. Monthly meetings,

chaired by the Chief Impact and Governance Officer, with representation drawn from subject matter experts and business leaders across the Society, attend these sessions to advise on strategy implementation.

The Society's Executive Committee received two reports in relation to climate-related activity in 2023, including updates on the net zero strategy, and our carbon footprint and offsetting activity.

In December 2022, the Board received the results of a carbon footprint 'deep dive' and an associated net zero roadmap, from leading climate change consultancy, ClimatePartner. In a clear demonstration of our commitment to tackling climate change by reducing our operational emissions, the Board agreed on a set of clear targets for 2023 and beyond.

Ownership for responding to the financial risk of climate change risk rests with the Risk Directorate with overall responsibility for meeting the Society's net zero ambitions resting with the Chief Impact and Governance Officer.

### Supply Chain Governance

Seeking to be a sustainability-focused organisation includes our supply chain. The Society has a Supplier Code of Conduct, which suppliers are expected to adhere to. This Code on Conduct includes information on checks made on suppliers prior to onboarding, and expectations of suppliers to develop their own plans to ensure they operate sustainably. This is done through a questionnaire on their social and environmental commitments.

### In 2023 the Society;

- Included a carbon reduction target in its variable pay scheme for all colleagues with oversight provided by our Remuneration Committee. This forms part of the Society's Strategic Key Performance Indicators (SKPIs)
- Implemented the Impact Working Group to oversee the carbon reduction activities and measure progress against the Society's net zero ambitions
- Continued to provide oversight, through ERC and BRC, on the agreed suite of Key Risk Indicators to monitor the financial risk of climate change
- Provided training and awareness to the Society's senior leadership team on our carbon footprint and key areas of emissions
- Developed a sustainable supply chain framework to ensure that sustainability considerations are embedded into the Society's procurement policy and approach
- Continued to recognise the importance of climate change to the Society's colleagues through regular climate-related communication. A colleague-led network continues to draw strong representation across the Society





At the start of our net zero journey, we set a target of becoming certified 'carbon neutral' (from 2021) and net zero in our business operations by 2030. These ambitions have now evolved \* but still form part of a wider strategic view of 'creating additional value by investing in and building a strong Environmental, Social and Governance (ESG) proposition'.

Elements of the ESG proposition are detailed in our Environmental Policy, outlining our plans to reduce our operational carbon footprint, which represents an SKPI for the business. We are currently creating a detailed carbon reduction roadmap including a corporate carbon footprint assessment. This will inform specific strategies and help devise policies for us to become a more environmentally sustainable business.

\*read an update on this on page 22

# Strategy

## Delivered to date

With a Head Office in Cardiff, 53 branches and 15 agencies spread across Wales and the Welsh Borders, we recognise that our operations have an impact on the environment that contribute to climate change. As mentioned above, as part of our commitment to achieve 'net zero' operational emissions, Principality partnered with Climate Partner in 2021 to help us better understand our operational carbon footprint.

They have supported us in identifying those parts of our operations that materially contribute to our footprint, by gathering and measuring the relevant data following the Greenhouse Gas Protocol Corporate Accounting and Reporting Standard (GHG Protocol).

A large proportion of our leased vehicle fleet used to run on diesel fuel, but following the update of our Company Car policy, we now have only one diesel vehicle remaining, which will be replaced with a lower-emission vehicle when the lease expires in October 2024. All other vehicles have been changed to either petrol hybrid or fully electric vehicles. Our aspiration is to move to a fully electric fleet, but this is largely dependent on the development of an effective infrastructure for charging electric vehicles across Wales and the rest of the UK.

In 2023, we continued to embed sustainability into the procurement process and our value chain to understand our suppliers' commitment to limiting their environmental impact. Our Supplier Code of Conduct requires them to continually seek ways to maximize the efficient use of raw materials and natural resources and minimise waste and pollution. In 2021 we contracted with Hellios, a due diligence platform, where a community of 50+ financial services organisations define standardised supplier assurance criteria across a number of risk areas, including ESG. The data received from Hellios is used by Principality to risk assess suppliers and obtain Scope 1, 2 & 3 emissions data. As at the end of 2023, 65% of our suppliers have completed the due diligence via Hellios and we are working offline with the





remaining companies to gather the appropriate data. In Q2 2024, an ESG scoring tool will be built into the Heliios platform to score the ESG position of suppliers against other comparable peers.

In October 2023 we provided a number of our Supplier Performance Managers across the business with bespoke training on how to engage suppliers in a discussion on setting emissions targets and starting a data collection process. This was supplemented with the development of a bespoke Sustainable Supply Chain toolkit to be shared with our suppliers, providing guidance on where to start and where to find relevant support.

To demonstrate our commitment to reducing our impact on the planet, in 2023 we included a carbon reduction target into our variable pay award for colleagues, for the first time. In order for this to be achievable, we had to engage colleagues and give them the tools to understand what climate change is, its effects, and what they can do to help reduce it. This meant building on the good work we started back in 2021 with the launch of mandatory carbon awareness training for all colleagues, helping to improve knowledge of what actions and activities contribute to climate change and how they can reduce their own carbon footprint both at home and at work. While nearly all colleagues have received this training, we have built on all of their feedback to recently refresh the learning modules to make them even more engaging and inspiring. The new videos were soft-launched to colleagues during Energy Savings Week in January 2024 and will be more formally uploaded to our new learning experience platform when launched later this year and included in part of the new colleague onboarding process.

TCFD Report

This mandatory training has been augmented with other more informal opportunities to engage on the subject, including livestream Lunch & Learn events with thought leaders and key practitioners in the climate issues space and will include more exposure to climate-related content as we build a more holistic engagement and education-led approach to broader ESG activities. We have a number of colleague-led networks, and Planet Friendly, our environmental network, provides the space for colleagues to engage in a climate action community, make climate smart choices, and focus on the practical skills that can create change within the organisation and beyond.

In 2021, Principality Commercial launched a £20m fund to support the development of low-carbon housing in Wales. The Green Development Fund offers housing developers financial incentives for the delivery of low to zero-carbon housing developments. This has been utilised and we are looking to launch the next tranche of this product later in 2024. In 2022, we also launched a 25-year term loan product to specifically support Housing Associations with their sustainability ambitions. This is proving popular with housing associations in Wales, an example of this being an ESG-linked loan of £50m to Pobl Group in 2023, which is being used to build new affordable and accessible homes, using the latest sustainable building materials and technologies, offering more people in Wales the opportunity to own and rent their own home.

# Understanding the risks of climate change



We recognise that climate change is a complex and inherently systemic issue, particularly difficult to model given the long-term nature of the risks. It has potential implications across a number of risks defined through the Enterprise Risk Management Framework (ERMF). We've identified the financial risks associated with climate change and plan to monitor our exposure through the current ERMF.

Climate change will either manifest itself as a physical risk - including acute risks (such as extreme weather-related events), and chronic risks (such as sea-level rise); or transition risk - including policy and legal risks, technology risks, market risks, and reputational risks. We also consider climate-related opportunities, including resource efficiency, energy sources, products and services, markets and resilience.

## Physical risk

Physical risks relate to the increasing severity and frequency of climate and weather-related events that may severely damage property and other infrastructure, disrupt business supply chains, impact agricultural output and more broadly can lead to loss of life and population migration. This reduces asset values, results in lower profitability for organisations, damages public finances, and increases the cost of settling underwriting losses for insurers. Indirect effects on the macroeconomic environment, such as lower output and productivity and increased costs, exacerbate these direct impacts.

## Transition risk

Transition risks arise from the adjustment towards a carbon-neutral economy and require significant structural changes. The transition will, among other things, prompt a reassessment of a wide range of asset values, a change in energy prices, and a potential fall in income, credit worthiness and wealth of some borrowers. In turn, this may result in credit losses for lenders and market losses for investors. However, the transition to a carbon-neutral economy also presents opportunities for the financial sector.

## Qualitative analysis

Physical risks are relatively well recognised, but we believe that the scope and materiality of transition risks are less well understood. The acute and chronic impacts of physical risks have been considered, but crystallisation would occur over the long term. The potential impact of a number of transition risks were considered, including government policy, market sentiment and legal and technology risks. Policy change is expected to represent the highest risk as the implementation of proposed government policies has the potential to influence the value of the housing stock.

## Scenario analysis

Scenario analysis does not predict the future, but it allows us to better understand the impact of climate change and how it could affect our company. Scenario analysis is a critical tool for strategic planning, risk management and assessing our strategic resilience. To understand fully the risks associated with properties currently held as security in support of the Society's mortgage portfolio, we partnered with Hometrack and others to capture relevant physical and transition risk data. Physical risk data includes an assessment of the likelihood of flooding (data provided by Ambiental) and subsidence and coastal erosion (data provided by TerraFirma). Transition risk data uses EPC ratings for currently mortgaged properties, with Hometrack sourcing the data from the Department for Levelling Up, Housing and Communities (DLUHC).

The Intergovernmental Panel on Climate Change (IPCC) has derived Representative Concentration Pathways (RCPs) which were used to assess the impact of physical risk on the book, with Hometrack data using the following pathways for their modelling:

RCP	CO <sub>2</sub> Emissions	Global Temp	Net Zero
2.6	Halved by 2050	Unlikely to exceed 2°C (in line with Paris Accord)	Achieved by 2070
6.0	Peak in 2080	More likely to exceed 2°C by 2100	Not Achieved
8.5	Continue on current trajectory	As likely as not to exceed 4°C increase by 2100	Not Achieved

We use this approach to undertake scenario analysis each year to re-assess whether our current climate-related risk management controls are sufficient, and as part of this we'll continue to upskill our internal stakeholders on the impacts of climate change.

## In 2023 the results of our scenario analysis identified the following impacts:



### Physical risk impact

Physical risks related to climate (i.e. flood, subsidence and coastal erosion) have been identified within the current portfolio and scenario analysis has been used to assess the change in risk over time and approximate the potential financial impact.

### Financial risk impact

The risks in the most severe scenario are not considered material at this stage. We will monitor exposure in the future and determine whether any changes to strategy or policy are warranted.

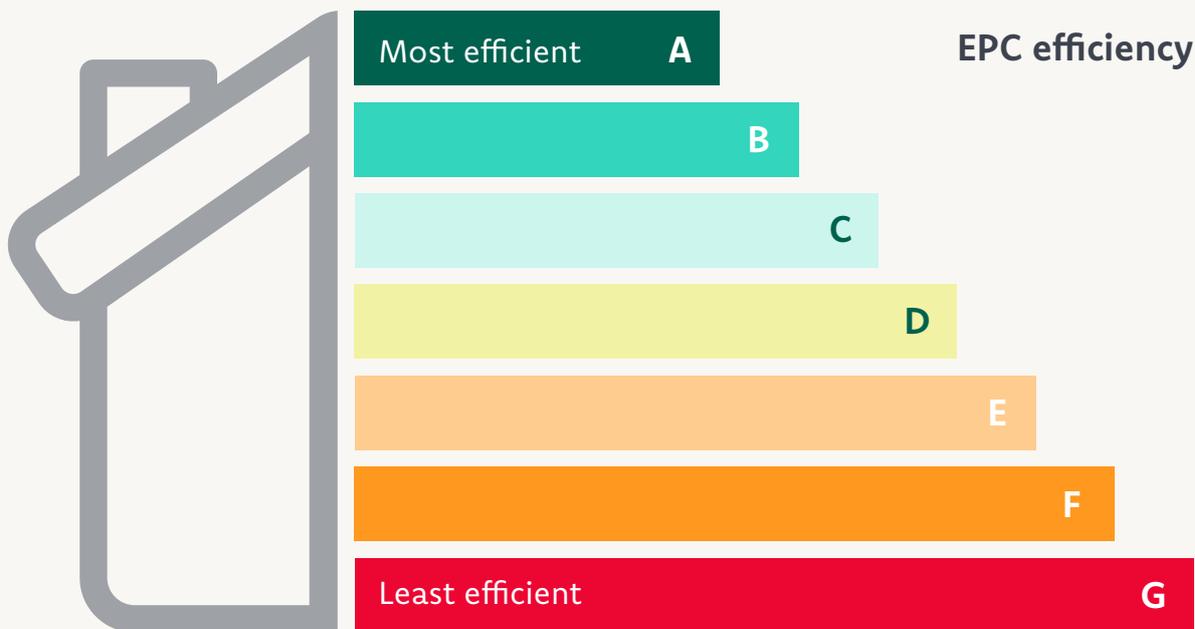
### Transition risk impact

Potential transition risks are broad, with little available data from which to quantify impacts. The Society's analysis was therefore driven by data availability and potential impacts assessed, based on current knowledge.

Potential changes to EPC (Energy Performance Certificate) legislation meet these criteria, as the Government could make changes in order to influence CO<sub>2</sub> emissions. We recognise that there is already legislation in place setting minimum EPC ratings for Buy-to-Let properties, which could be tightened and/or expanded in the future.

The EPC data for properties is available in order to complete this analysis. Emissions included in the EPC data are also needed to calculate Scope 3 financed emissions for the total mortgage portfolio.

Our analysis was based on the assumption that the Government applies a policy for minimum EPC rating for domestic properties, where currently the minimum for rented properties is band E. A severe but plausible scenario where all domestic properties are required to have an EPC of at least C has been modelled.



### EPC Overview

EPCs were first introduced by the UK government in 2007 in England and Wales to meet the requirements of the EU Directive on the energy performance of buildings. Initially, these were included as part of the Home Information Pack (HIP), required for sales of properties of four bedrooms or more. The requirement to have an EPC for buildings that are either sold or rented has been extended to include all domestic and commercial properties and is still a key requirement.

An EPC rating is a review of a property's energy efficiency and a score is allocated to each property ranging from A (most efficient) to G (least efficient). The expected energy costs and carbon emissions are calculated taking into consideration the building structure, heating and hot water systems, and lighting.

#### There are some limitations to using EPCs:

- They are only valid for ten years
- They are only required when a homeowner sells a property
- They can be sensitive to fluctuations in energy prices
- Improvements made to a property following purchase are not reflected in the EPC rating
- The rating does not reflect the level of emissions generated from a property, much of which is determined by the behaviour of the occupants
- The rating does not reflect all electrical consumption, only lighting

In order to perform an analysis of the transition risk of the mortgage book, EPC ratings were acquired for all properties where available and an analysis of the distribution of the book was completed. Scenario analysis was based on the introduction of a minimum EPC rating and the potential impacts it may have on our mortgage book. There is a great deal of uncertainty around the implications of transition risk, and as such we will incorporate them in future assessments once more detail is known.

From a governance perspective, we will continue to disclose our risk management process and key roles and responsibilities for oversight relating to climate-related risks and opportunities; continue to learn from and implement best practices from other organisations and third parties with expertise in climate change; and continue to consider how the Board includes climate-related issues in decision making on strategy and performance.



# Risk management



Climate change creates implications and impacts right across our business. Rigorous and consistent risk management practices are embedded across our Enterprise Risk Management Framework (ERMF) and are designed to identify, assess and mitigate risks to minimise their potential impact and support the achievement of our business strategies.

We recognise risks associated with climate change will persist and evolve over time. As changes to our climate, such as global temperatures and more frequent extreme weather events intensify, so will the materialisation of risk at a regional and global level. We continue to identify, evaluate and review existing and emerging risks to ensure our risk management framework develops in tandem with the environment in which we operate.

The framework outlines the strategic approach for risk management and provides an integrated and holistic view of vulnerabilities and risks across the business by describing responsibilities, delegation of authorities, and the methods by which risks are identified, measured, monitored and controlled. Principal risks within our ERMF are assessed, where relevant, using climate change as an optic to better understand any potential impact, and our assessment process ensures that management can review and understand whether the risk exposure is within or outside the agreed appetite.

There are two key elements to the assessment:

- A forward-looking view of the **probability** of an event occurring
- The **impact** should the event occur

Each principal risk is evaluated against criteria which measure the probability of that risk occurring and the impact it would have on the business. The assessment considers a number of variables and a quarterly residual value is derived for each risk that considers, amongst other things, the potential impact of climate change.

When assessing the impact of climate change on our principal risks, the approach remains proportionate. We will consider the potential transition risks, for example those that arise from the adjustment towards a low-carbon economy, and physical risks that relate to the increasing severity and frequency of climate-related events.

The framework to support climate-related risk is integrated within our three lines of defence approach to risk management. The day-to-day operations, our first line of defence, have primary responsibility for the identification, assessment, management and monitoring of climate change-related risks. The Risk function is the second line of defence, providing oversight and challenge to the first line to ensure we remain alert to changes in the environment and meet our regulatory commitments. The Internal Audit function is the third line of defence providing risk-based independent assurance of our controls and management of climate-related risks. All three lines are responsible for considering both the financial and non-financial risks of climate change when performing their roles.

As our understanding of the risks posed by climate change evolves, we will assess the potential impact on the business, and our customers, by reference to a range of factors that include the following:

Our culture and risk management philosophy reflects a strong awareness of the current and emerging risk landscape that could affect the delivery of our strategy.

We will continue to focus on developing appropriate measures for our key climate-related risks and opportunities and evolving our climate risk management information to monitor our key risk indicators whilst monitoring transition risk related to government policy.

Risk category	Potential impact (Transition & Physical risk)
<p><b>Credit risk</b> The risk that borrowers or counterparties do not meet their financial obligations as they fall due</p>	<ul style="list-style-type: none"> <li>• Climate Change could affect unemployment numbers through various aspects. Job displacement, changes in demand of labour and impacts on vulnerable communities.</li> <li>• Impact on house prices due to government policy such as the stipulation of minimum EPC ratings</li> <li>• Physical damage to property caused by climate change e.g. flooding</li> <li>• Impact of increased household insurance premiums leading to uninsured and/or underinsured homes</li> </ul>
<p><b>Operational risk</b> The risk of loss arising from inadequate or failed internal processes, systems, human error or from external events</p>	<ul style="list-style-type: none"> <li>• Physical damage to the property portfolio including branches and offices</li> <li>• Loss of systems and data due to physical impacts</li> <li>• Increased use of our services resulting from the crystallisation of a physical risk</li> <li>• Availability of employees during a physical event and the impact this would have on our ability to provide Members with a service</li> <li>• Impact on the supply chain in relation to costs and their ability to provide agreed services due to physical impacts</li> <li>• Reconsideration of third-party relationship due to their attitude to climate change risk</li> </ul>
<p><b>Conduct risk</b> The risk of poor outcomes to customers or an adverse effect on market integrity arising from the actions and behaviours of employees and the Society as a whole</p>	<ul style="list-style-type: none"> <li>• Potential for increased levels of complaints and disputes because climate-related physical or transition risks result in poor customer outcomes</li> </ul>
<p><b>Liquidity and funding risk</b> Liquidity risk is the risk that the Society has insufficient funds to meet its obligations as and when they fall due. Funding risk is the risk that the Society is unable to access funding markets or is only able to do so at excessive cost</p>	<ul style="list-style-type: none"> <li>• Reduced savings balances due to economic impact of climate change risk on customer wealth</li> <li>• Reduced wholesale funding access following lower investor appetite due to negative perception of Principality in relation to the management of risks associated with climate change</li> </ul>
<p><b>Business risk</b> The risk arising from changes to the business model and the risk of the business model or strategy proving inappropriate due to macroeconomic, competitive, geographical, regulatory or other factors</p>	<ul style="list-style-type: none"> <li>• Reputational damage caused by a negative perception of Principality and its perceived response to the climate risk agenda</li> <li>• Managing and meeting member expectations</li> <li>• Macroeconomic market impacts arising from physical or transition events</li> </ul>
<p><b>Interest rate risk</b> The risk that the value of income derived from the Society's assets and liabilities is adversely impacted because of changes in interest rates</p>	<ul style="list-style-type: none"> <li>• Climate policies implemented by regulators could potentially lead to changes in Interest Rates as investors adjust expectations for future economic growth and inflation</li> </ul>
<p><b>Solvency risk</b> The risk that the Society does not maintain sufficient capital resources in excess of minimum regulatory requirements</p>	<ul style="list-style-type: none"> <li>• Deterioration of balance sheet assets following physical impacts or as a consequence of a fall in the value of collateral held to support mortgage loans</li> </ul>

# Metrics and targets



Having accurate data is fundamental to being able to properly measure and monitor our climate-related risks so that we have a good understanding of where we are starting from and can make a more informed assessment of where we want to be.

In 2023, we continued to review and improve the quality of our data to make it even more accurate and we will continue to do so going forward. This improved data quality has resulted in some changes to our emissions figures, detailed below. Where appropriate, we have explained the reason for these changes.

## Operational emissions

Scope 1 emissions are created directly by the Society from self-generated heat and from our fleet vehicles. Scope 2 emissions are indirect emissions from purchased electricity and Scope 3 covers all other indirect emissions from our operations occurring from sources that are not owned or controlled by the Society. Financed emissions relate to the emissions of the financed element of properties included in the mortgage portfolio, and whilst part of Scope 3 (category 15), are reported separately here.

Principality has always fulfilled its obligations under the government's Streamlined Energy & Carbon Reporting (SECR) initiative and outputs have been monitored closely. This year our Scope 3 emissions have expanded again and now include all applicable categories.



2023 emissions summary	Total [t CO <sub>2</sub> e <sup>1</sup> ]	Total [%]
<b>Scope 1</b>		
<b>Direct emissions from company facilities</b>	<b>255.24</b>	<b>4.7</b>
Heat (self-generated)	253.09	4.7
Combustion	2.15	-
<b>Direct emissions from company vehicles</b>	<b>7.87</b>	<b>0.1</b>
Vehicle fleet	7.87	0.1
<b>Scope 2</b>		
<b>Purchased electricity for own use<sup>1</sup></b>	<b>1.36</b>	<b>-</b>
Electricity (vehicle fleet)	1.36	-
Electricity	-	-
Purchased heating, steam, and cooling for own use	-	-
Heat (purchased)	-	-
<b>Scope 3</b>		
<b>Purchased goods and services</b>	<b>3,747.05</b>	<b>69.7</b>
Externally calculated service emissions	3,623.89	67.4
Print products	108.32	2.0
Electronic devices	9.11	0.2
Office paper	3.76	0.1
Water	1.71	-
External data centre	0.26	-
<b>Capital goods</b>	<b>623.37</b>	<b>11.6</b>
Capital goods	623.37	11.6
<b>Employee commuting</b>	<b>514.68</b>	<b>9.6</b>
Employee commuting	299.19	5.6
Home office	215.49	4.0
<b>Fuel- and energy-related activities</b>	<b>86.70</b>	<b>1.6</b>
Upstream emissions heat	42.29	0.8
Upstream emissions electricity	41.95	0.8
Upstream emissions vehicle fleet	2.46	-
<b>Business travel</b>	<b>77.61</b>	<b>1.5</b>
Rental and private vehicles	44.12	0.8
Hotel nights	15.52	0.3
Rail	13.96	0.3
Flights	4.01	0.1
<b>Upstream transportation and distribution</b>	<b>50.34</b>	<b>0.9</b>
Other upstream transports	50.34	0.9
<b>Waste generated in operations</b>	<b>8.85</b>	<b>0.2</b>
Operational waste	8.71	0.2
Transport to disposal facility	0.14	-
<b>Overall results</b>	<b>5,373.07</b>	<b>100</b>

<sup>1</sup>Calculated using the market-based method. Emissions calculated using the location-based method are 506.00 t CO<sub>2</sub>e

## 2022 v 2023 comparison

In 2022 we did not have our full carbon footprint available at the time of reporting, but this was calculated later in 2023, enabling us to provide a full year-on-year comparison:

Emission Source	2023		2022		Change YoY	
	Emissions [t CO <sub>2</sub> e]	Share %	Emissions [t CO <sub>2</sub> e]	Share %	Emissions [t CO <sub>2</sub> e]	%
<b>Scope 1</b>	<b>263.11</b>	<b>4.8</b>	<b>300.69</b>	<b>3.6</b>	<b>-37.58</b>	<b>-12.5%</b>
<b>Direct emissions from company facilities</b>	<b>255.24</b>	<b>4.7</b>	<b>290.97</b>	<b>3.5</b>	<b>-35.73</b>	<b>-12.3%</b>
Heat (self-generated)	253.09	4.7	241.55	3.0	11.54	+4.8%
Combustion	2.15	-	3.51	-	-1.36	-38.7%
Refrigerant leakage	-	-	45.91	0.5	-45.91	-100.0%
<b>Direct emissions from company vehicles</b>	<b>7.87</b>	<b>0.1</b>	<b>9.72</b>	<b>0.1</b>	<b>-1.85</b>	<b>-19.0%</b>
Vehicle fleet	7.87	0.1	9.72	0.1	-1.85	-19.0%
<b>Scope 2</b>	<b>1.36</b>	<b>-</b>	<b>0.25</b>	<b>-</b>	<b>1.11</b>	<b>+444.0%</b>
<b>Purchased electricity for own use</b>	<b>1.36</b>	<b>-</b>	<b>0.25</b>	<b>-</b>	<b>1.11</b>	<b>+444.0%</b>
Electricity (charging for vehicle fleet)	1.36	-	0.25	-	1.11	+444.0%
<b>Scope 3</b>	<b>5,108.60</b>	<b>95.1</b>	<b>7,836.98</b>	<b>96.3</b>	<b>-2,728.38</b>	<b>-34.8%</b>
<b>1. Purchased goods and services</b>	<b>3,747.05</b>	<b>69.7</b>	<b>3,917.11</b>	<b>48.2</b>	<b>-170.06</b>	<b>-4.3%</b>
Operational Expenditure (all other)	3,623.89	67.4	3,767.3	46.3	-143.41	-3.8%
Print products	108.32	2.0	131.35	1.6	-23.03	-17.5%
Electronic devices	9.11	0.2	7.66	0.1	1.45	+18.9%
Office paper	3.76	0.1	5.97	0.1	-2.21	-37.0%
Water	1.71	-	4.47	0.1	-2.76	-61.7%
External data centre	0.26	-	0.36	-	-0.10	-27.8%
<b>2. Capital Goods</b>	<b>623.37</b>	<b>11.6</b>	<b>3,058.92</b>	<b>37.6</b>	<b>-2,435.55</b>	<b>-79.6%</b>
Capital Expenditure	623.37	11.6	3,058.92	37.6	-2,435.55	-79.6%
<b>3. Fuel- and energy-related activities</b>	<b>86.70</b>	<b>1.6</b>	<b>86.32</b>	<b>1.0</b>	<b>0.38</b>	<b>+0.4%</b>
Upstream emissions heat	42.29	0.8	41.36	0.5	0.93	+2.2%
Upstream emissions electricity	41.96	0.8	42.44	0.5	-0.49	-1.2%
Upstream emissions vehicle fleet	2.46	-	2.52	-	-0.06	-2.4%
<b>4. Upstream transportation</b>	<b>50.34</b>	<b>0.9</b>	<b>49.08</b>	<b>0.6</b>	<b>1.26</b>	<b>+2.6%</b>
Delivery of letters, leaflets, and cheques	50.34	0.9	49.08	0.6	1.26	+2.6%
<b>5. Waste generated in operations</b>	<b>8.85</b>	<b>0.2</b>	<b>20.49</b>	<b>0.2</b>	<b>-11.64</b>	<b>-56.8%</b>
Operational waste	8.71	0.2	18.80	0.2	-10.09	-53.7%
Transport to disposal facility	0.14	-	1.69	-	-1.55	-91.7%
<b>6. Business travel</b>	<b>77.61</b>	<b>1.5</b>	<b>41.31</b>	<b>0.5</b>	<b>36.3</b>	<b>+87.9%</b>
Rental and private vehicles	44.12	0.8	27.67	0.3	16.45	+59.5%
Rail	15.52	0.3	7.47	0.1	8.05	+107.8%
Hotel nights	13.96	0.3	6.17	0.1	7.79	+126.3%
Flights	4.01	0.1	-	-	4.01	+100.0%
<b>7. Employee commuting</b>	<b>514.68</b>	<b>9.6</b>	<b>663.75</b>	<b>8.1</b>	<b>-149.06</b>	<b>-22.5%</b>
Home Office	299.19	5.6	351.29	4.3	-52.10	-14.8%
Employee Commuting	215.49	4.0	312.46	3.8	-96.97	-31.0%
<b>Overall results</b>	<b>5,373.07</b>	<b>100.0%</b>	<b>8,137.92</b>	<b>100.0%</b>	<b>-2,764.85</b>	<b>-33.9%</b>

It is really positive news that our full carbon footprint decreased by 33.9% in 2023.



The most significant contributor to this is the reduction in emissions from our capital expenditure, as we moved away from buying physical goods related to the 2021/22 Principality House refurbishment and home working setup, and spent more on services and consultancy, which typically have lower emissions.

We have also seen reductions in our operational expenditure, employee commuting and home working emissions, although a significant proportion of this is a result of data quality improvements. However, the continued focus on reducing the quantity of paper we send did yield a positive result, saving 23 t CO<sub>2</sub>e and we look forward to seeing this number reduce even further in 2024.

We are also pleased to see our carbon footprint per colleague continue to reduce:

Year	Footprint per colleague (tonnes CO <sub>2</sub> e)
<b>2023</b>	<b>4.20</b>
<b>2022</b>	<b>6.75</b>
<b>2021</b>	<b>11.12</b>

As stated on page 17, in 2022 we were unable to report on all our purchased goods and services at the time our TCFD was published so the table below gives a like-for like comparison of what was reported last year:

Scope	Category	Description	2023 emissions (tCO2e)	2022 emissions (tCO2e)	Change in emissions (tCO2e)	Change in emissions %
1	1	Heat (self-generated)	255.24	241.55	13.69	5.7
1	2	Refrigerant leakage	0.00	45.91	-45.91	-100
2	1	Electricity (vehicle fleet)	1.36	0.25	1.11	444.0
3	1	Print products	108.32	131.35	-23.03	-17.5
3	1	Electronic devices	9.11	5.97	3.14	52.6
3	1	Office paper	3.76	4.47	-0.71	-15.9
3	1	Water	1.71	0.36	1.35	375.0
3	1	External data centre	0.26	7.66	-7.40	-96.6
3	3	Upstream emissions heat	42.29	41.36	0.93	2.2
3	3	Upstream emissions electricity	41.95	42.44	-0.49	-1.2
3	3	Upstream emissions vehicle fleet	2.46	2.52	-0.06	-2.4
3	4	Upstream transportation and distribution	50.34	49.08	1.26	2.6
3	5	Waste generated in operations	8.85	20.50	-11.65	-56.8
3	6	Rental and private vehicles	44.12	27.67	16.45	59.5
3	6	Hotel nights	15.52	6.17	9.35	151.5
3	6	Rail	13.96	7.47	6.49	86.9
3	6	Flights	4.01	0.00	4.01	100.0
3	7	Employee commuting	299.19	351.29	-52.10	-14.8
3	7	Home office	215.48	312.46	-96.98	-31.0
<b>Total</b>			<b>1,117.93</b>	<b>1,298.48</b>	<b>-180.55</b>	<b>-13.9</b>



For the last two years we have been a carbon neutral organisation, offsetting all our reported emissions with carbon credits. However, with no globally agreed definition of carbon neutrality, it is increasingly difficult to understand what different organisations mean by this term.

As a result, ClimatePartner, who have supported us with this work for the past three years, have created a new certification process for its clients. 'ClimatePartner certified' is a certification awarded to clients who have evidenced the following five steps of climate action:



#### Measure carbon footprint

– calculate carbon footprint in line with the requirements of the Greenhouse Gas Protocol. Update annually to make climate action successes visible



#### Set reduction targets

– short and long term



#### Implement reductions

– implement measures to start reducing emissions



#### Finance climate projects

– Fund verified projects that demonstrably save or capture CO<sub>2</sub> and promote the UN Sustainable Development Goals. The financing of global climate projects is urgently needed in addition to the reduction of emissions



#### Communicate transparently

– Make commitment and action taken visible to all stakeholders

## Beyond Value Chain Mitigation (BVCM)

For the last two years we have offset our corporate carbon footprint using carbon credits. However, this only focuses on offsetting emissions from our direct value chain, but does little to address systemic challenges in the carbon reduction industry and falls short of creating active change in the carbon mitigation industry.

As a result, Principality is adopting the Beyond Value Chain Mitigation (BVCM) framework, which is designed to broaden our understanding and approach to mitigating climate impact. We will extend our climate efforts beyond our immediate operations and contribute to societal efforts for achieving net-zero emissions by investing in a wider scope of climate mitigation efforts. Often, new technologies and approaches that aim to move this industry forward are drastically under-funded because the cost per ton of offsetting is prohibitive

for most but BVCM provides different frameworks to address this. By financing technological innovation we can scale up clean technologies for effective, long-term carbon reduction and removal.

Principality has chosen the Money-for-Ton approach, financing carbon mitigation techniques based on a predefined price per ton of our unabated emissions for 2023. This means, for every ton of CO<sub>2</sub>e we produced in 2023, we will put £15 towards financing a climate project, totalling £100,000. Transparent reporting will allow us to focus on real change and support global climate initiatives in line with SDG 13 for climate action. We are currently in the process of purchasing our BVCM carbon credits and will publish more information on which project we choose on our website when the transaction is complete.

# Financed emissions



Category 15 of Scope 3 emissions relates to investments. For Principality, this means the financed emissions from our retail mortgage portfolio. As discussed in the Strategy section of this document, despite its limitations, we believe that EPC data currently represents the best available methodology for calculating carbon emissions generated from a property.

The table below gives an overview of the carbon emissions of the retail mortgage portfolio. Total CO<sub>2</sub> emissions per square metre are calculated for the mortgage portfolio using property level data and adjusted by the loan-to-value (LTV) ratio to derive estimated carbon emissions financed by the Society.

## Methodology

The calculation of Scope 3 financed emissions aligns to the PCAF (Partnership of Carbon Accounting Financials) standard, using estimated carbon emissions based on EPC ratings. A weighted LTV of the mortgage is then applied to calculate the proportion of the property value financed by the Society.

PCAF guidance suggests using the property value at origination, but there are drawbacks of using this metric as it does not accurately reflect current financing for customers who have increased their borrowing as house prices have increased. Using a more recent house valuation would therefore give a better representation of the LTV ratio and estimated financed emissions of the book.

Property values for loans originated up to, and including, August 2023 have been derived through internal calculations using HPI (House Price Index). Loans originated after August 2023 retain their value at origination.

## Data quality score

A weighted data quality score of 3.49 has been calculated for financed emission data by:

- Using emissions data in publicly accessible EPCs available for approximately 76% of the total mortgage book. These are given a data score of 3.
- Interpolated EPC data across the remaining 24% of the portfolio. Properties without an EPC are assumed to have the same EPC characteristics as the properties with an EPC. These are given a data score of 5.

The calculation of the data score is based on allocating a score from 1 to 5 based on the accuracy of the data used. The closer the score is to 1 the higher the data quality. A score of 1 or 2 is based on actual building emissions, a score of 3 or 4 is based on estimated building emissions based on floor area, and a score of 5 is estimated building emissions based on number of buildings. Principality does not have access to actual building emissions, therefore a score closer to 3 would indicate higher data quality for the Society.

## Comments

Estimated total emissions have increased 0.03 M tCO<sub>2</sub>e per year from the 2022 disclosure (0.31 from 0.28) largely due to an increase in the number of properties, with a similar increase of 2kg CO<sub>2</sub>e per square metre per year (42.65 vs 40.89). Financed emissions have increased 0.19 kg CO<sub>2</sub>e per square metre per year since 2022, due to an increase in the average emissions of properties where loans have been advanced in the last 12 months. The data score has improved in 2023 due to a higher proportion of new business written having a valid EPC.

Scope 3 mortgage emissions:	2023			2022		
	Total	Owner Occupier	BTL	Total	Owner Occupier	BTL
<b>Property Metrics</b>						
Volume of Properties - With a valid EPC	60,390	42,773	17,617	55,078	37,855	17,223
Volume of Properties - Total book	79,890	57,988	21,902	75,904	54,039	21,865
Property floor area in million metres square (i) - With a valid EPC	5.42	4.03	1.39	4.95	3.61	1.34
Property floor area in million metres square (i) - Total book	7.18	5.47	1.73	6.83	5.15	1.70
<b>Absolute Scope 3 carbon dioxide emissions (CO<sub>2</sub>e) in million tonnes (Mt) per year (y) for mortgages</b>						
On properties with a valid EPC (ii)	0.23	0.17	0.06	0.20	0.14	0.06
On whole book using interpolated EPC data (iii)	0.31	0.23	0.08	0.28	0.20	0.08
Absolute carbon dioxide emissions in kilograms per square metre of floor area per year (kgCO <sub>2</sub> e/m <sup>2</sup> /y) using interpolated EPC data	42.65	41.77	45.19	40.89	39.32	45.11
<b>LTV weighted Scope 3 carbon dioxide emissions (CO<sub>2</sub>e) in million tonnes (Mt) per year (y) for mortgages</b>						
On whole book using interpolated LTV weighted data (iv)	0.17	0.13	0.04	0.14	0.12	0.04
LTV weighted carbon dioxide emissions in kilograms per square metre of floor area per year (kgCO <sub>2</sub> e/m <sup>2</sup> /y) using interpolated data (v)	23.89	24.37	22.26	23.70	23.56	23.78
Data Score (v)	3.49	3.52	3.39	3.55	3.60	3.42

[i] Total floor area is taken from the EPC reports and interpolated for the total book.

[ii] Calculations are based on number of mortgaged properties with a valid EPC. This is approximately 76% of the mortgage portfolio (up from 73% in 2022).

[iii] Calculations are based on estimating EPC data across the whole mortgage portfolio using interpolation based on housing data. The carbon dioxide emissions account for EPC covered emissions only (space and water heating, and lighting). Indirect emissions from other energy uses by the household have been excluded such as those resulting from the use of domestic appliances.

[iv] LTV adjustments have been applied to the total CO<sub>2</sub> emissions predicted for the whole mortgage book. The 2022 LTV breakdown has been re-stated.

[v] Data scoring aligns with PCAFs Global GHG Accounting and Reporting Standard, with 1 representing high data quality and 5 representing low data quality.

# Targets



Although we would like to set a target for the decarbonisation of the mortgage book, we do not believe it is possible to set a meaningful target until there is more certainty over the UK Government's policy and investment plans in relation to achieving its net zero commitment under the Paris Agreement.

We continue to support this initiative in a number of ways, including contributing to various working groups led by organisations such as UK Finance and the Building Societies Association to lobby and influence government policy on issues including the decarbonisation of the UK housing stock.

In June 2023, we made changes to our Valuers Guidance Notes to provide further clarity regarding the Modern Methods of Construction (MMC) that we would lend on, subject to receiving the relevant assurances and certificates of their durability. This has made it easier for both valuers and brokers to understand what we would accept, thereby making the process simpler for our customers and allowing us to support them in their quest for low-carbon living. Given the varying types of construction being used in the industry, we see this as an evolving piece of work.

## Principality has the following targets:

### 1. Net zero in Scopes 1 & 2 by 2030

### 2. Net zero in Scope 3

(excl. the mortgage book) by 2040, but with a significant reduction (>50%) being achieved by 2030

As a mutual building society, climate change action is at the heart of what we do – protecting and supporting our local, national and global communities. Our dedicated Sustainability Manager, now supported by a wider Impact working group, continues to drive this work forward across all areas of the business to identify where we can deliver positive change, big or small. However, as detailed in our Annual Report and Accounts, we know that to make a material reduction in our carbon footprint and achieve our net zero ambitions we're going to need to make big changes to our systems and processes. Realistically, some of these things may take years to implement before we start seeing the benefits.

One example is the need to update our systems and data so that we can better capture and act upon customer communication preferences. This should help us reduce the amount of paper we generate and send. We made 'Paperless by Default' a priority for 2023 and made good progress getting this long-term project off the ground.

At Principality, we consider ourselves an ethical organisation and strive to ensure that all ESG-related risks across the business are well managed. We are therefore working closely with ESG rating providers to ensure that this is reflected in our ESG assessment scores as far as possible.

## Summary

	Delivered to date	Current focus	Future deliverables
<b>Governance</b>	<p>Strategic KPI for carbon reduction and included as part of variable pay award</p> <p>Impact Working Group established</p>	Supporting carbon reduction initiatives and the production of a net zero transition plan	Refresher training for Board
<b>Strategy</b>	<p>Developed approach to climate change scenario analysis and reporting</p> <p>Developed relationships with third parties to supply climate-related data</p> <p>Use physical and transition risk analysis to inform decision making</p> <p>Guidance notes on MMR lending updated</p>	Continue to use physical and transition risk analysis to inform strategic decision making	<p>Explore further risks and opportunities</p> <p>Monitor and enhance understanding of physical and transition risks</p>
<b>Risk management</b>	<p>Assessed physical and transitional risks</p> <p>Amended current risk appetite statements</p> <p>Developed climate change risk appetite statement</p> <p>Developed suite of Key Risk Indicators (KRIs) for climate change risk</p>	<p>Monitor climate change risk through current risk framework</p> <p>Annual reporting of KRIs to Board Risk Committee</p>	Continue analysis of transition risks
<b>Metrics and targets</b>	<p>Data quality continued to improve</p> <p>Annual reduction target for 2023 achieved</p>	<p>Continued improvement of data quality for carbon footprint</p> <p>Active supplier engagement and use of supplier toolkit to reduce emissions from our value chain</p> <p>Continued focus on reducing paper-based customer communications</p>	<p>Continue to work with partners to develop and improve climate change reporting</p> <p>Future system enhancements to reduce reliance on paper communications to customers</p>



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