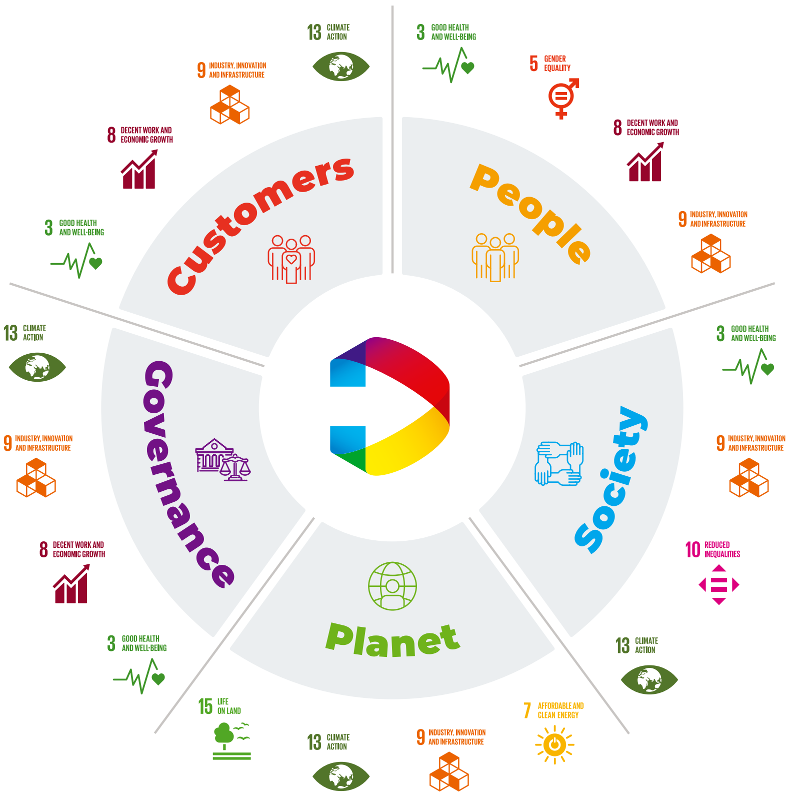
Sustainability

Building a sustainable future



We stand for insurance excellence because positive customer outcomes mean we can grow our business

We stand for being a diverse and inclusive employer because attracting and retaining talented people powers our business forward

We stand for being rooted in our communities because when they flourish so does our business

We stand for a greener planet because we're all in it together, it's our responsibility, and tackling climate change benefits our business, our people and society

We stand for a competitive and strong financial services sector because it's essential to being successful

In 2022, we continued to put in place sustainable initiatives to strengthen the business, whether it's being brilliant for customers, being an inclusive employer, giving back to our communities, protecting the planet or maintaining high standards of governance. The wheel on the previous page highlights how our five pillar Sustainability Strategy aligns to the United Nations Sustainable Development Goals ("SDGs") and the table below shows material issues which take into account our broad range of stakeholders.

Goals	Material issues	2022 outcomes	
Earn our customers' trust by demonstrating how we are acting in their interests	– Deliver great service – Communicate clearly and openly – Protect customers' data – Harness data and technology – Innovate sustainable products and services	**All of our front-line staff of more than 5,000 received vulnerable customer training which was nominated for a Learning and Performance Institute award**	**More than** **5,000**
Encourage a culture that celebrates difference and empowers people so that they can thrive	– Develop a diverse and inclusive workforce – Uphold good labour standards – Support employee wellbeing – Maximise employee engagement – Train and develop our people	**Ranked 20th on the Inclusive Top 50 UK Employers List**	
Use our expertise to improve outcomes for society and the communities we serve	– Improve social mobility – Increase road safety – Drive financial inclusion – Contribute to local economic development	**Through our Community Fund we engaged with 500 students to help younger people with their careers**	**500**
Protect our business from the impact of climate change and give back more to the planet than we take out	– Reduce our climate change impact – Reduce waste and optimise resources – Advance the low-carbon transition – Adapt to climate change	**The Science Based Targets initiative approved our carbon-reduction plans**	
Look to the long term for our stakeholders, build a reputation for high standards of business conduct and develop a sustainable business	– Control executive pay – Build strong Board governance – Manage our supply chain responsibly – Tax strategy and transparent disclosure – Invest responsibly	**We were awarded a Fast Payer Accreditation Award by Good Business Pays, recognising our role in supporting our suppliers**	

Customers

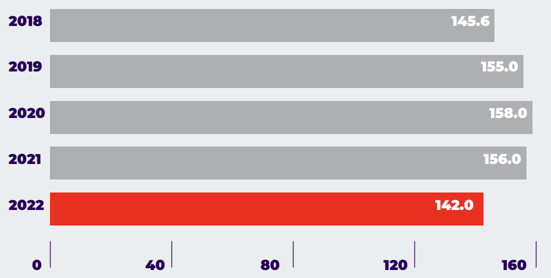
Our mission is to earn our customers' trust by demonstrating how we are acting in their interests

This year we've seen customers realise the benefits of efficient digital-first journeys and, during a period where cost of living challenges have impacted so many, we introduced and implemented support mechanisms for those facing economic difficulty.

Net Promoter Score

We pride ourselves on our Direct Line brand NPS. While our 2022 performance experienced a dip on previous years due to economic headwinds creating parts, labour and hire car supply challenges, our score remains above the industry average.[1]

Net Promoter Score[2] – Direct Line Brand



Customer support

Helping our customers during the cost of living crisis

In line with our customer-first approach, we have introduced several measures to support those facing financial difficulty currently and for the foreseeable future.

We are asking customers to discuss with us their needs so we can look to offer the most appropriate support; this may include reviewing levels of cover or considering any alternative products.

Vulnerable customer training nomination

More than

5,000

All front-line staff have received enhanced vulnerable customer training in 2022

Building on our CONNECT training programme used by our consultants to support customers, we have developed enhanced training for colleagues to support vulnerable customers.

All 5,000 of our front-line staff have completed this training and this programme was nominated for a Learning and Performance Institute Award in 2023.

Notes:
1. Institute of Customer Services organisation ranking score.
2. Please see Net Promoter Score KPI on page 23 for further information.

Churchill Essentials product

This year we launched a new Essentials motor product using our Churchill brand. Available only on price comparison websites, the product has been designed to meet the needs of customers looking for a comprehensive product, but does not include certain elements such as new car replacement, loss of keys or personal belongings that are typically part of a standard comprehensive product. It's an alternative for customers who may be looking for great value in a stripped-back motor insurance policy.

"Working in our agile model, a number of teams worked collaboratively to launch our Churchill Essentials product."

Bhanu Shekar Gutta, Software Engineer

Brilliant for customers every day

Improving the claims experience for customers

When customers make a claim that's when it matters most, because we step in and support people facing difficult moments.

That's why we're continuing to deliver easy digital-first journeys to give people peace of mind. Motor customers can now register 100% of claims types across the vast majority of our brands and partners online. In 2023, we will be looking to introduce the capability for motor customers to be able to track the status of their claim online from start to finish whether they are waiting for their car to be fixed or waiting for a cash settlement.

Delivering an excellent motor claims experience is good for customers and our business:

- Churchill is ranked as the leading insurance brand for digital service and claims[1].
- In Motor, over 85% of customers score us highly (8-10) on whether they would recommend Direct Line to friends and family[2].
- Nearly 90% of motor customers score us highly (8-10) for how easy it is to claim[2].

Helping our vulnerable customers

We have developed a suite of online tools to support our colleagues to identify and address a vulnerability when speaking to a customer. One of these tools encompasses a grid of vulnerabilities across headings such as life event, financial resilience, financial capability and health. When a customer mentions a key word, our agents can click on the specific tile and are prompted with a number of considerations and options on how best to interact with them and provide the required service adjustments.

Plain Numbers

Building on our successful partnership with Plain Numbers last year, in which we trialled their approach to reduce technical language and clarify numbers to simplify our communications with customers, we signed up to a cross-industry partnership led by the Association of British Insurers in February 2022, to further our activity and understanding in this area and to train more colleagues as practitioners in the Plain Numbers method.

Tackling fraud

We have a strong track record in identifying and dealing with fraudulent activity, helping us deliver better outcomes for customers. In the last five years our counter-fraud measures have avoided £650 million being paid out to fraudsters and we've been rated as the top industry performer for personal motor fraud savings, personal motor applications for fraud, and property application fraud savings by the Association of British Insurers[3].

Supporting rescue customers

From 2021, Green Flag enhanced its policy for actively prioritising customers who might need immediate support, such as lone or vulnerable travellers on the roadside at night or families with young children. Over the course of the year over 40,000 priority incidents were reported, which included over 5,000 vulnerable customers. Our drivers attended these vulnerable customers incidents in under 49 minutes, with customers communicating with us through the phone and on our app, where they could track where the rescue vehicle was.

Notes:
1. Lumivo Q2 2022.
2. Research conducted by TLF based on customer perception at end of claim.
3. Source: 2021 ABI General Insurance Fraud Benchmarking.

People

Our mission is to encourage a culture that celebrates difference and empowers people so that they can thrive

Over 2022, our focus was on building future skills, continuing to push forward the promotion of diversity and inclusion in the business, and engaging with our people during the cost of living crisis.

Building future skills

Our commitment to training people for the jobs of the future was taken to a new level in 2022. We launched our Ignite academies which incorporate apprenticeship programmes to develop the vital skills needed to serve our increasingly tech-savvy customers. 170 new apprentices are already working across Data, Customer Service and Data, Software Engineering, and Pricing and Underwriting, joining the 224 we already had. We also launched our Data Academy so all colleagues can grow their data capability and learn new skills, with over 1,000 engaging in courses, lunch and learn sessions and using resources from the website.

Minimum salaries

While we seek to ensure a good pay proposition for all our people, we have shown a clear focus over a number of years on lifting the salaries for our lowest-paid colleagues. That focus meant in April 2022 our minimum salary rose by 6.7%, seeing pay for a 37.5 hour week rise to £20,800 from £19,500[1]. During 2022, for Direct Line Group employees, our minimum salary was 7.7% above the Living Wage Foundation's National Real Living Wage (as set in November 2021 for roles outside of London) and 12.3% above the Government's statutory National Living Wage (effective 1 April 2022 figure for those aged 23 or over).

In August 2022, we announced a further pay increase of 5% to all our employees (excluding senior management) from January 2023, meaning our minimum salary rose to £21,840 p.a. (based on a 37.5hr working week). This stands at 2.8% above the Living Wage Foundation's National Real Living Wage (as set in September 2022 for roles outside of London) and will be 7.5% above the Government's statutory National Living Wage (effective 1 April 2023 for those aged 23 or over).

Engaging with our people

Engaging with colleagues as the key stakeholders that they are is at the heart of how we run our business.

In addition to our Executive Committee participating in regular "Ask Anything" sessions, both in person and online, during which they address business performance and issues affecting it and where any colleague can ask a question or put forward their ideas, three of the most important ways we engage with our people are:

1. Employee Representative Body ("ERB") – The ERB, which comprises colleagues from across business areas and locations, meets regularly with the leadership of the Group, including the CEO, to discuss issues and proposals which have, or may have, an impact on colleagues.

2. DiaLoGue – DiaLoGue is our employee engagement tool that we use to survey all colleagues three times a year. Findings provide both a snapshot and trends not only of all-colleague opinion but also findings for specific teams, allowing solutions to be tailored to specific needs. Response to these surveys is consistently high (over 80%).

Note:
1. Subject to satisfactory performance and excluding apprentices in DLG Auto Services who receive different rates of pay.

Examples of engagement with our people having resulted in business action include:

	Issue raised	Action Taken
Cost of living	We talked with our ERB to get their insight on how our people are being affected and how best to make a meaningful difference.	**Boosting the pay of lowest paid:** In April we boosted the pay of our lowest-paid colleagues, increasing the minimum salary by 6.7% to £20,800. **Earlier pay increase and one off payment** In the summer we announced a 5% pay increase for all our people with effect from 1 January 2023, meaning colleagues received the increase three months earlier than usual and in January 2023 a one-off cost of living payment of £1,000 was announced for colleagues in salary bands 1 and 2 and those in other bands earning less than £40,000. **Increased visibility of help available** We promoted the broader financial support available to our people including emergency support, everyday budgeting, and planning.
Menopause	Our Diversity Network Alliance ("**DNA**") strands raised the challenges that women can face having open conversations and accessing support when perimenopausal or menopausal.	**New guidance, training and internal awareness building** Our DNA strands worked with HR and The Menopause Charity to launch new guidance on perimenopause, menopause and andropause. It provides people managers with help on how to have good conversations and practical information on effective workplace adjustments. This has been embedded with training for people leaders and our HR Advisory team, alongside internal communications activity to broaden knowledge and end stigma.
New London hub	We discussed the proposed 2023 move from our site in Bromley to a new location near London Bridge with our ERB, DNA strands and with individual colleagues via their people leaders to identify both the broad implications and the issues for specific colleagues.	**Travel assistance policy** We agreed a revised Travel Assistance Policy to help colleagues with any increased travel costs for a period of one year. **Inclusive spaces** The different needs of colleagues have been incorporated into the design of the new office, for example a quiet room, multi-faith prayer room and nursing room.

3. Diversity Network Alliance (DNA) – Our seven employee networks are a key driver of diversity and inclusion across our business. They focus on the following areas: Belief, Life (families and carers), LGBTQ+, Neurodiversity & Disability, REACH (race, ethnicity and cultural heritage), Social Mobility and Thrive (gender).

Strength in diversity & inclusion

We believe that improving diversity and inclusion needs enhanced policies and practices, along with changing mindsets and culture. Across 2022, we have continued to address both.

Our focus on culture and behaviours builds deeper understanding of issues, together with the commitment to drive change, at all levels of our business.

Recruitment and promotion

Our approach to inclusive hiring aims to attract the widest possible range of people and protect against bias. Amongst the measures we follow, we:

- Use inclusive language analytics tools
- Remove unnecessary qualification or experience requirements
- Use anonymised CVs for senior roles[1]
- Train recruiting managers on inclusive hiring

Policies and support

We want our policies and guidance to support people to be the best they can, recognising life impacts work and work impacts life. This year, we have updated or introduced additional support on:

- Flexible working
- Menopause
- Anti-bullying & harassment
- Pregnancy loss
- Workplace adjustments

Reverse mentoring

This year, we concluded a year-long reverse mentoring programme which provided senior leaders with deep insights into the barriers faced by marginalised communities and in turn enabled them to offer valuable career advice and guidance.

Accelerating inclusion

In 2022, we developed a new Accelerating Inclusion programme to grow the capability and skills of all our people to be more inclusive. Over 1,000 colleagues have already participated in the programme, which will continue over 2023.

"The Neurodiversity and Disability network has gone from strength to strength this year, supporting our 350+ members with insight sessions and a new parents network."

Molly Welsh, Counter Fraud Intelligence Handler and Neurodiversity & Disability Network Co-lead

Increasing the representation of women in senior leadership

Improving the representation of women at the senior levels of our business is ongoing but we are proud of the progress we have made.

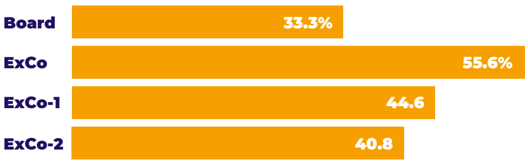
Note:
1. Anonymised CVs do not apply to Executive Committee and Board Roles.

Women in Finance

Having achieved our Women in Finance target of 30% women in senior management[1] back in 2019 we chose to adopt an ambitious stretch target of 35% by the end of 2022. On 31 December 2022, 31.3% of our senior leadership were women. While we missed our stretch target we believe the process of target setting has had value and driven our internal work to improve gender representation.

Senior women in leadership representation %

Penny James agreed with the Board to step down as Direct Line Group CEO in January 2023. The numbers below reflect the representation of women in senior leadership following this change.



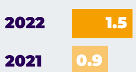
Our long-term focus on investing in women means we have strengthened representation at the most senior levels of our business. In 2023, we will be setting our next set of targets and our focus is on building the pipeline at the mid-levels as we work towards gender parity.

Growing ethnic minority and Black representation in leadership

At the end of 2020, we set ourselves a challenging deadline of 31 December 2022 to meet our first ever set of targets to increase ethnic minority and Black representation in leadership. Although we missed our ethnic minority goal, we achieved our Black representation target and we believe the process of target setting has had value and driven our internal work to improve representation, which is why we will be setting new targets for this in 2023.

Growing ethnic minority representation from 10% to 13%

Growing Black representation from 0.5% to 1.5%



Activity we are undertaking to shift the dial includes:

- Building a stronger pipeline of ethnic minority and Black talent, especially in areas where the jobs of the future are, because we want to future-proof our activity. This includes work experience, mentoring and skills building programmes that target these communities for our Ignite academy apprenticeship programmes.
- Investing in a new development programme focused on supporting high-potential Black women, with diverse role models from across sectors and a specific focus on navigating through some of the challenges that can be faced by Black female leaders.

Gender pay gap

Last year our mean gap widened by 3.2 percentage points and our median gap by 6.1 percentage points. Our pay gap continues to be low compared with the broader financial services sector, but we want to see that gap close. We are comfortable that we don't pay people differently because of their gender and believe that the way to reduce the gap in the medium- to long-term is to continue with our work to address the disproportionate representation of women at certain levels and in certain areas of our business.

Our 2022 gender pay gap showed:

Pay Gap[2]

	Mean	Median
2022	**19.3%**	**20.3%**
2021	16.1%	14.2%
2020	17.2%	15.4%

Bonus Gap

	Mean	Median
2022	**46.7%**	**45.4%**
2021	45.9%	34.0%
2020	47.9%	36.3%

% of employees receiving bonus

	Men	Women
2022	**83.1%**	**82.6%**
2021	72.7%	60.6%
2020	73.5%	62.4%

Notes:

1. Our Women in Finance Charter definition of senior management is based on our internal grading structure and represents approximately the 1.2% most senior colleagues in our business.
2. The Gender Pay Gap shows the difference in average pay between women and men. This is different to equal pay, which is women and men receiving the same pay for work of equal value. Our reporting is based on a snapshot date of 5 April 2022.

Ethnicity pay gap

This year, we are publishing our ethnicity pay gap for the second time. We are voluntarily disclosing this data. We have chosen to do so to hold ourselves to account and to inform diversity and inclusion initiatives across the business. Comparing the data of 2022 and 2021, our mean gap decreased by 0.5 percentage points and our median gap increased by 1.8 percentage points, with both remaining low.

As with the gender pay gap, we are comfortable that we don't pay people differently because of their ethnicity and believe that the way to reduce the gap in the medium- to long-term is to continue with our work to address the disproportionate representation of ethnic minority and black colleagues at certain levels and in certain areas of our business.

Pay Gap[3]

	Mean	Median
2022	**2.6%**	**9.7%**
2021	3.1%	7.9%

Bonus Gap

	Mean	Median
2022	**40.9%**	**19.1%**
2021	32.9%	11.8%

% of employees receiving bonus

	White	Ethnic minority
2022	**84.6%**	**74.6%**
2021	68.2%	58.6%

Our mean and median pay gaps by ethnicity

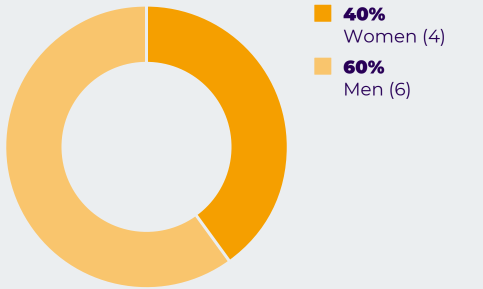
We recognise that different communities can have different experiences, so we have further broken down the data to understand pay gaps for our Black, Asian, Mixed and other ethnicity colleagues versus White colleagues. It's important to note that when pay gap data is based on a smaller number of individuals, it can vary significantly over time due to colleague changes during the year.

	2022	
	Mean	Median
Black	**11.2%**	**11.0%**
Asian	**0.7%**	**16.1%**
Mixed race	**0.4%**	**4.9%**
Other	**2.3%**	**(6.1%)**

3. The Ethnicity Pay Gap shows the difference in average pay between ethnic minority, Black and White colleagues. This is different to equal pay that is ethnic minority and White colleagues receiving the same pay for work of equal value. Our reporting is based on a snapshot date of 5 April 2022 and 87% of colleagues that have shared their ethnicity with us. As we continue to encourage colleagues to share their ethnicity with us, changes to disclosure will impact the numbers we report.

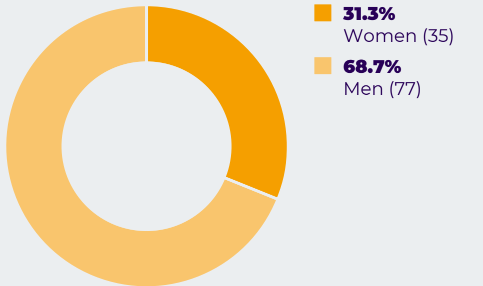
Gender diversity of our Board

As of 31 December 2022



Gender diversity of senior leadership

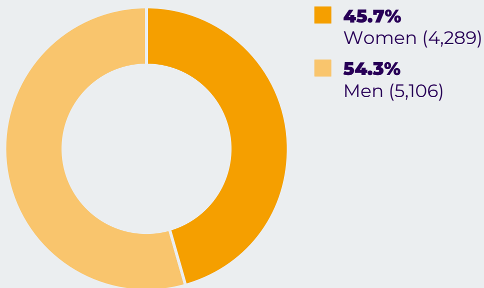
As of 31 December 2022



Gender diversity of senior leadership figures based on 2022 Women in Finance Charter reporting

Gender diversity of all employees

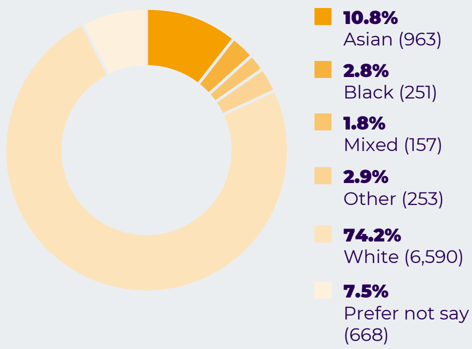
As of 31 December 2022



Excludes an estimated 0.5% colleagues who identify as non-binary, gender-fluid or other gender due to data reporting constraints

Ethnicity of all employees

As of 31 December 2022



Excludes 5.9% of colleagues who have not submitted an option for ethnicity

For more information on leadership gender diversity, including gender diversity of the Board see pages 99 and 100.

Society

Our mission is to use our expertise to improve outcomes for society and the communities we serve

This year, we were excited to take the next step in our social mobility journey, focusing our Community Fund on the aim of building a more inclusive and equitable Britain. We additionally looked to provide support to those in need at home and abroad, with our colleague-led donations for charitable causes around the UK, and contributions made to the Disasters Emergency Committee efforts in Ukraine and Pakistan.

Giving back

Over the course of the year, we supported a variety of charitable causes. This included:

- Donating £150,000 in total to the Disasters Emergency Committee campaigns in Ukraine and Pakistan
- Our colleague-led Community and Social Committees ("**CASCs**") distributing £100,000 to local causes
- Sponsoring the NSPCC's Great Chefs dinner, which raised almost £300,000 to help children around the UK
- Our Diversity Network Alliance giving £90,000 to organisations aligned with their diversity and inclusion goals

Road safety

Our campaigning for improved road safety continued, working in partnership with the Parliamentary Advisory Council on Transport Safety ("**PACTS**"). An updated report[1] was published in 2022 which set out actions to increase seat belt wearing rates in the UK and save preventable loss of life on roads. The report highlighted that wearing a seat belt reduced the risk of death for drivers in a road collision by some 50%.

Prompt payment code

As a responsible business, we are a longstanding signatory of the Department for Business, Energy and Industrial Strategy's Prompt Payment Code, a voluntary code of practice for businesses to ensure payments are made to suppliers on time. During the last year, when cost of living challenges were significant and the importance of swift payments were even more recognised, we were awarded a Fast Payer Accreditation Award by Good Business Pays, recognising our role in supporting our suppliers, big and small.

Human rights

Our aim is to be a force for good and we want to build a reputation for being an ethical business which drives our commitment to have employment practices and policies that exceed the Universal Declaration of Human Rights. We are committed to ensuring modern slavery is not present in our supply chain. Our risk profiling, including specific requirements within our due diligence and assurance processes, incorporates the Modern Slavery Act 2015.

Our 2022 tax contribution

We act in accordance with all applicable tax laws and regulations and meet our responsibilities both as a contributor of corporate taxes and as a collector of taxes on behalf of HMRC. In 2022, the Group's net tax contribution was £803.9 million, which includes the Group's direct and indirect taxation.

Our customers	IPT	**£389.4m**
Our suppliers	VAT	**£14.8m**
Our people	PAYE NIC	**£102.4m**
Our operations	Other taxes including business rates	**£5.9m**
	Irrecoverable VAT	**£256.4m**
	Employers NIC	**£44.8m**
Our performance[2]	Corporation Tax	**£(9.8)m**

HM Treasury

£803.9m[3]

Net tax contribution

Society

- Public services
- Healthcare
- Infrastructure
- Welfare
- Education
- Defence

Notes:
1. Source: https://www.pacts.org.uk/pacts-briefing-seat-belts-time-for-action/
2. The Group made a loss before tax of £45.1 million, resulting in a corporation tax credit of £5.6 million.
3. The Group's total tax contribution in 2022, including direct and indirect tax contributions.

Community Fund 2022

Since the start of 2020, our Community Fund has helped over 300 charitable causes, supporting over 200,000 families and individuals facing adversity, mental health challenges and food poverty. Building on these achievements, and with so many of our colleagues feeling passionately about social mobility, we were delighted to focus our Community Fund in 2022 with a new ambition: to build a more inclusive and equitable Britain.

Partnering with three organisations, Envision, Springpod and Young Professionals, we have launched a programme of engagement, to use our expertise across the business to help equip younger people with key career skills.

"It was fantastic to mentor students with our Community Fund and give back to younger people starting on their career journeys."

Timon Pryce, Principal Pricing Analyst Developer

Reach

of the programme

500

students engaged to improve employment skills

100%

were eligible for free school meals

85%

were from an ethnic minority background

58%

identified having a parent/parents from a working-class occupation

150+

colleagues signed up to be a mentor, participate in work experience or attend an insight event

Work experience

In-person and virtual events focusing on employability skills and workshops on data and technology were held, giving participants the opportunity to learn about important career skills

Mentoring

Highlighting the variety of roles on offer at Direct Line Group, colleagues from Finance to Technology to Marketing gave students an insight into what their day to day job entailed

Insight events

Hosted across several office sites across the country, sessions on topics such as how an insurance company works, building a sustainable business, and how to run a marketing campaign took place

Direct Line Group Community Fund

Impact

after taking part in the programme

93%

felt they understood how an insurance company operates

83%

felt more able to ask someone for a connection to build their professional network

74%

felt more confident to apply for jobs

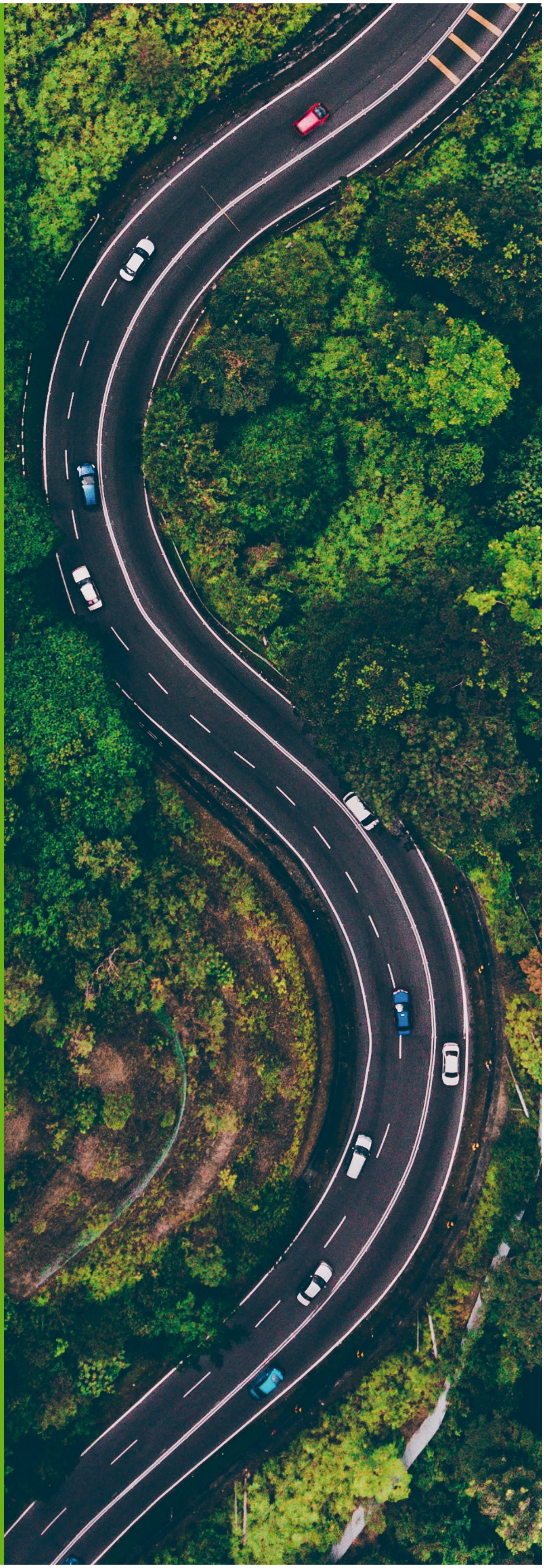
To measure the impact of the programme, students were asked to complete a survey prior to, and after, participating in a Community Fund activity. A few of the key stats are highlighted above.

In 2023, the programme will continue with the aim of engaging with more students to help build a more inclusive and equitable Britain.

Planet

Our mission is to protect our business from the impact of climate change and give back more to the planet than we take out

We believe in supporting customers to make the transition to a low carbon world, climate risk mitigation, and in playing our part in reducing our carbon footprint.



There are three steps which guide our approach:

Step 1

Disclose to track progress

We disclose our carbon emissions because it's how we hold ourselves to account and helps us to find practical solutions to reduce our footprint.

We have measured and disclosed our Scope 1 and 2 emissions since 2013 and in recent years made it clear how these emissions are split between our office sites and accident repair centres. We have also expanded the categories we report under Scope 3, including our Supply Chain, and for the second year running, our Homeworking emissions, recognising that more colleagues are working from home.

Step 2

Commit to tangible actions

We signed up to Race to Zero where companies set emission reduction targets in line with limiting global warming to 1.5 degrees.

We have set ambitious Science-Based Targets, approved by the Science Based Targets initiative ("**SBTi**"), as we aim to become a Net Zero business by 2050. The most carbon intensive areas of our business – our accident repair centres, supply chain and investments – all have plans in place.

Step 3

Offset while we reduce

While we transition to Net Zero, we currently offset emissions under our direct control by investing in three carbon reduction projects around the world.

While we transition to Net Zero, we currently offset our Scope 1 and 2 emissions as well as elements of our Scope 3 emissions under our direct control by partnering with Climate Impact Partners[1], an organisation that is dedicated to tackling climate change and improving lives by financing, developing and managing carbon reduction projects.

What does Net Zero mean for us?

We aim to become a Net Zero business by 2050. Our plan covers operational emissions (Scope 1 and 2) and our investments.

The business also prioritises the following Strategic Management Actions:

- **Electric vehicles –** improving our capability to support the transition to EVs.
- **Supply Chain –** implementing a Supply Chain Sustainability Programme to engage and influence suppliers.
- **Flood resilience –** engaging with policymakers on the importance of flood defences and helping to shape thinking around resilient repairs.
- **Underwriting footprint –** evaluating the impact of climate change on our underwriting footprint so that we can manage risks to our business and help inform strategic decision making.

Note:
1. Previously known as ClimateCare.

Our approved SBTi plans

We have now stepped up our ambitions. In November 2022, we were delighted to become one of the first personal lines general insurers in the UK to have our Science-Based Targets approved by the SBTi, meaning we now have ambitious carbon reduction plans on which we will publicly report our progress each year.

We have greater understanding of our carbon footprint. A proportion of our Scope 1 and 2 carbon emissions comes from our offices and accident repair centres, where we have the largest insurer-owned garage network in the UK supporting motor customers.

We have five Science-Based Targets – one target covers our operational emissions and a further four targets cover our investment portfolio. The five Science-Based Targets approved by the SBTi and which we are targeting are:

Our Science-Based Targets

	Covering	Target	How we do it
Operational emissions (Scope 1 and 2)	**Our buildings and garage network** Including our 22 accident repair centres, the largest insurer-owned network in the UK.	1. Reduce emissions 46% across our office estate and accident repair centres by 2030[1]	– Electrifying heating and cooling systems using renewable energy. – Replacing diesel with hydrogenated vegetable oil in recovery trucks. – Removing gas consumption in spray paint booths by moving to renewable electricity.
Investment portfolio (Scope 3)[2]	**Corporate Bonds** The largest asset class in our investment portfolio and typically short duration holdings.	2. Align our scope 1 + 2 portfolio temperature rating to 2.08°C by 2027[3,4] 3. Align our scope 1, 2 + 3 portfolio temperature rating to 2.31°C by 2027[3,4]	– Tilt reinvestment towards companies taking serious action to reduce emissions. – Work with our external investment managers to engage with investees to encourage ambitious emission reduction target setting.
	Commercial Property A relatively small allocation within the investment portfolio consisting of prime UK commercial properties. **Real Estate Loans** A small allocation within the investment portfolio consisting of short dated loans backed by UK commercial properties.	4. Reduce emissions from our commercial property portfolio 58% per square metre by 2030[1,5] 5. Reduce emissions from our real estate loans portfolio 58% per square metre by 2030[1,5]	– For commercial property, our external asset manager aims to improve the energy efficiency of buildings, engage with tenants to disclose energy use data (implementing green lease clauses where possible), encourage tenants to set emissions reduction targets, including Science-Based Targets. – For real estate loans, our external managers will encourage borrowers to improve the energy efficiency of buildings, and to take energy efficiency of buildings into account when originating loans, and the ability of the borrower to share tenant energy use data.

For more information on the five Science-Based Targets approved by the SBTi which we are targeting, see pages 84 and 85.

Taking action with our supply chain

In 2021, we launched our Supply Chain Sustainability Programme, outlining our plan between now and 2030 to engage and influence suppliers so we can make the transition to a pathway consistent with a 1.5°C scenario. This programme includes our Sustainable Sourcing Approach, encouraging our principal suppliers within our direct control to sign up to SBTi targets or an equivalent. We are also requesting information on what efforts firms have made to measure their carbon footprint across scopes 1, 2 and 3 and their plans to reduce emissions, including targets, so we can evaluate whether it is viable to change our sourcing approach on appropriate contracts.

We have also chosen to set an internal emissions reduction target while we wait for the publication of the Science-Based Net Zero Targets for Financial Institutions from the SBTi, which is expected later in 2023.

Notes:
1. Compared to a 2019 baseline.
2. Covering 75% of our investment and lending activities by monetary value as of 2019.
3. Using a Temperature rating method, we've targeted to align our scope 1 + 2 portfolio temperature score from 2.44°C in 2019 to 2.08°C by 2027 and our scope 1 + 2 + 3 portfolio temperature score from 2.80°C in 2019 to 2.31°C by 2027.
4. The temperature score for corporate bonds is the implied level of warming above pre-industrial levels to which our corporate bond portfolio is aligned based on the CDP's temperature rating methodology.
5. Commercial real estate targets were set using the SBTi sectoral decarbonisation approach for real estate which uses the IEA ETP 2017 Beyond 2°C scenario.

Our climate journey so far

2013
Began measuring our carbon footprint

2014
Electricity for all our offices and repair centres purchased from renewable sources

2016
Our first electric vehicle charging points installed

2018
New energy efficient office opened in Bristol

2020
Offset all our direct emissions

2021
Direct Line launches its first EV bundle for customers

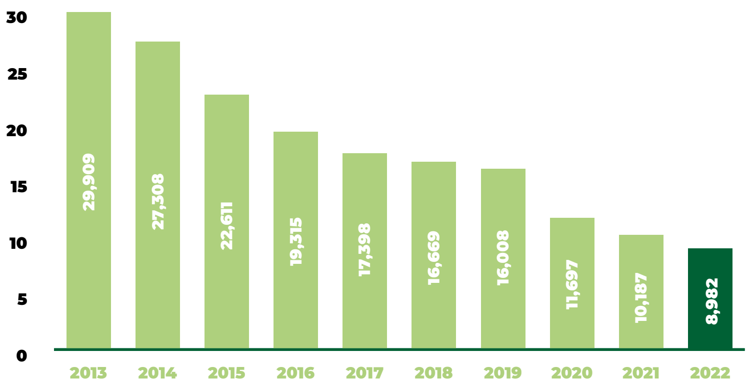
2022
SCIENCE BASED TARGETS
DRIVING AMBITIOUS CORPORATE CLIMATE ACTION

One of the first personal lines insurers in the UK to have its Science-Based Targets approved by the SBTi

Since 2013, we have made progress to reduce our carbon footprint:

- Reduced our energy consumption by 56% since 2013[1]
- Procured 100% renewable electricity for our operations since 2014
- Diverted 100% of our office waste from landfill

Greenhouse gas emissions (tCO_2e)[2,3,4]



Energy consumption (kWh)[3,4]

	2022	2021
Electricity	**12,686,882**	14,856,315
Gas	**21,485,898**	24,286,023
Total	**34,172,780**	39,142,338

Supporting electric vehicle customers

Last year, our Direct Line brand launched a 'Making electric easy' campaign which included a bundle of electric vehicle charging benefits and discounts (in partnership with Zoom EV), alongside insurance cover for batteries and charging cables for all new business customers. Due to successful uptake, the bundle was extended for another year and made available to all Direct Line Motor customers, as well as broadened to include a discounted home charger by Zaptec and wider access to an EV help and guidance line (run by Zoom EV).

Notes:
1. Reduction in energy consumption is reported on a like-for-like basis.
2. Total Scope 1 and 2 emissions. The 2021 and 2019 figures differ from previously reported figures, found on page 72 of the Group's 2021 Annual Report and Accounts, following the validation of our Science-Based Targets.
3. 100% of GHG emissions and energy consumption reported relates to operations, all of which are based in the UK.
4. Data is reported in compliance with the Streamlined Energy and Carbon Reporting ("**SECR**") requirements (see page 85).

Biodiversity

This year, we funded tree planting on a flood prevention scheme in Yorkshire to replace the trees we remove when home insurance policyholders make subsidence claims[1]. Working in partnership with nature recovery charity Heal, we also provided a loan to acquire a 460 acre site near Bruton in Somerset to support rewilding of the land.

Energy efficiency measures[2]

In 2022, we continued to invest in energy efficiency measures and focus on the most carbon-intensive areas of the business which will help us work towards meeting our Science-Based Targets.

Building on last year's activity, we have:

- Rolled out our hydrogenated vegetable oil ("**HVO**") trial in our recovery trucks to 90% of our Auto Services sites. This has saved 543 tCO_2e in 2022.
- Fitted energy-saving LED lighting to a further six repair centres meaning nearly 70% of our Auto Services sites have now received these upgrades.
- Installed a Power Factor Corrector in our Birmingham Auto Services site to maximise the efficiency of our electrical supply on-site. In 2021, installation at our Crawley repair centre delivered a 13% improvement in energy efficiency.

"I'm proud to be part of a team that helped us to receive validated Science-Based Targets. Part of our plan involves replacing diesel in our trucks with sustainable, hydrogenated vegetable oil."

Carrie Loftus, Sustainability Programme Manager

Our investments

All external investment managers are signatories of the United Nations Principles for Responsible Investment ("**UN PRI**"), which ensures that Environmental, Social, and Governance criteria are integrated into the investment process. For investment-grade corporate bond portfolios, as an added measure, we require that managers maintain an average MSCI ESG rating equivalent to or higher than that of the ESG-weighted reference index each portfolio is managed against.

We have set ourselves the target of achieving net zero emissions from the investment portfolio by 2050 as part of our alignment with the Race to Zero campaign on climate change. During 2022, we achieved an important milestone on this journey by having our Science-Based Targets approved.

In addition, we are keeping our target of reducing the GHG emissions intensity of our corporate bond portfolio by 50% by 2030 versus a 2020 baseline as a backward-looking indicator, to make sure emissions are reducing at the required pace over time to achieve our long term net zero goal.

We also require the below exclusions and preferences:

- The exclusion of any companies with a MSCI low-carbon transition score, indicating assets could be economically stranded.
- The exclusion of companies involved in thermal coal activity, either mining or power generation, at greater than 5% of revenues.
- Managers instructed to prefer investments in green bonds where the risk return characteristics are similar to conventional bonds.

Group emissions

We believe accurate measurement and transparency can guide the business in making targeted interventions as part of our carbon reduction strategy. We implemented a number of test and learn activities, and continue to innovate and explore a range of solutions. We have provided a comparison of emissions data for Scope 1, 2 and 3 with greater clarity of the activities under our direct control, as well as our supply chain emissions.

100% of the emissions reported in the table on page 69 relate to our operations, all of which are based in the UK. The data is reported in compliance with the SECR requirement to disclose annual global GHG emissions (see page 85 for more information).

Notes:
1. Yorkshire Flood Alleviation Scheme at Broughton Hall Estate as part of a rewilding project to help grow the White Rose Forest.
2. Data is reported in compliance with the SECR requirements (see page 85).

Definitions

Scope 1: This covers direct emissions from owned or controlled sources. For example, our office sites throughout the UK using gas boilers, the paint booths in our Auto Services sites currently relying on gas powered processes, and our fleet vehicles.

Scope 2: These are indirect emissions. They are emissions associated with the production and transmission of energy we eventually use as a company across our office and Auto Services sites. For example, the production of the electricity we buy to heat and cool our buildings generates emissions.

Scope 3: These are indirect emissions that occur in the value chain to support our company operations. For example, employee commuting, activities related to the disposal of waste, and the goods and services we purchase to fulfil customer claims as part of our supply chain.

Scope 1	**2022**	2021	2020	2019 baseline
Office sites[1]	**1,023**	1,220	1,339	1,418
Auto Services[1,2]	**5,506**	5,812	6,472	7,981
Total (tCO_2e)[1,2]	**6,529**	7,032	7,811	9,399

Scope 2	**2022 Location-Based[3]**	**2022 Market-Based[3]**	2021 Location-Based[3]	2021 Market-Based[3]	2020 Location-Based[3]	2020 Market-Based[3]	2019 baseline Location-Based[3]	2019 baseline Market-Based[3]
Office sites	**1,089**	**0**	1,372	0	2,176	0	4,516	0
Auto Services	**1,364**	**0**	1,783	0	1,710	0	2,093	0

	2022	2021	2020	2019 baseline
Total (tCO_2e)	**2,453**	3,155	3,886	6,609
Total Scope 1&2 (tCO_2e)[1,2]	**8,982**	10,187	11,697	16,008
Of which: office sites (tCO_2e)[1]	**2,112**	2,592	3,515	5,934
Of which: Auto Services (tCO_2e)[1,2]	**6,870**	7,595	8,182	10,074
Scope 3 emissions under our direct control				
Fuel and energy-related activities[1]	**1,518**	2,586	2,332	2,459
Waste generated in operations[1,2]	**2,523**	1,990	413	3,358
Business travel – air travel	**195**	28	198	928
Business travel – hotel night stays	**120**	34	75	469
Business travel – rail	**160**	29	63	410
Employee commuting[1,4,5]	**7,227**	5,962	1,450	3,176
Of which: homeworking emissions[5]	**5,583**	5,501	–	–
Upstream leased assets[1,6]	**189**	110	63	514
Upstream transportation and distribution of auctioned vehicles[1]	**1,890**	655	625	4,173
Downstream leased assets[7]	**1,552**	964	–	–
Total (tCO_2e)[1,2]	**15,374**	12,358	5,219	15,487
Total emissions under our direct control (tCO2e)[1,2,8]	**24,356**	22,545	16,916	31,495
Scope 3 – supply chain				
Total procured goods and services (tCO_2e)[1,2,9]	**244,316**	268,696	144,114	294,080
Direct Line Group carbon footprint (operational control)				
Total (tCO_2e)[1,2,8]	**268,672**	291,241	161,030	325,575
Of which: under our direct control[1,2,8]	**24,356**	22,545	16,916	31,495

Notes:

1. The 2019 reported baseline differs from our previously reported baseline, found on page 72 of the Group's 2021 Annual Report and Accounts, following the validation of our Science-Based Targets.
2. The 2021 reported figures differ from our previously reported figures, found on page 72 of the Group's 2021 Annual Report and Accounts, following the validation of our Science-Based Targets.
3. Figures for Scope 2 use standard location-based methodology. We follow GHG Protocol to disclose both location and market-based figures; and as we have secured our energy from 100% renewable sources since 2014, our Scope 2 market-based results are nil.
4. Employee commuting is based on estimated UK national averages, not actual individual methods of transport of Direct Line Group employees commuting.
5. Homeworking emissions are reported under the Employee Category in line with GHG Protocol.
6. Upstream leased assets refer to (1) leased office space locations where Direct Line Group does not directly control the energy provision as it is included in the service agreement, (2) Auto Services pods in retail car park locations and (3) Auto Services courtesy cars emissions.
7. Includes Auto Services' courtesy cars emissions which were previously reported under Scope 1. 2021 data represented accordingly.
8. Total of Scope 1 and 2 emissions and Scope 3 emissions under our direct control.
9. In accordance with the GHG Protocol under which we report, the following are excluded from the total: operational control activities already detailed under 'Scope 3 emissions under our direct control'; cash payments to customers or other insurance companies/legal firms as compensation; intragroup transfers between our operating companies for financial accounting purposes as the actual purchase of goods and services to our third-party suppliers is already captured; and reinsurance costs to third-party reinsurers as this is a financing transaction.

Reporting methodology

We comply with the applicable greenhouse gas reporting requirements contained within Schedule 7, Part 7 of the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 (as amended) and apply the GHG Protocol Corporate Accounting and Reporting Standard (revised edition) to calculate our emissions, which includes emissions associated with electricity consumption. We use the operational control method to define the boundary for consolidating GHG emissions.

Our carbon emissions are calculated by an external third party and reviewed internally. The calculation method used for our 2022 emissions reporting remains consistent with prior periods and with the reporting standards stated above. For the year ended 31 December 2022, we received independent assurance for our Scope 1 and 2 emissions reporting.

Intensity metric

We monitor and report the intensity metric of emissions[1] per £ million annually of net earned premium and in 2022 we expanded our reporting to include a measure of emissions[1] per average number of employees[2]. These measure how efficiently we provide our insurance products and allow us to compare our performance year-on-year and against other insurance companies.

Year	GHG emissions (tCO_2e) per £ million of net earned premium	GHG emissions (tCO_2e) per average number of employees for the year[2]
2022	**3.0**	**0.9**
2021[3]	3.4	1.0
2020	4.0	1.1
2019[3,4]	5.4	1.4
2018	5.4	1.5
2017	5.5	1.6
2016	6.4	1.8
2015	7.7	2.1
2014	9.1	2.4
2013	9.5	2.4

Offsetting projects

From 2020 to 2023, we pledged support to three projects which deliver high social impact benefits to communities, families and the environment. During the last year, progress has been made in all these initiatives with our support contributing to:

- The manufacturing and distribution of water filters, helping to provide safe drinking water to communities and schools across Kenya. The project also reduces the need for people to boil water to make it safe to drink, which requires the burning of unsustainable energy sources such as wood or charcoal.
- The production and distribution of 'Bondhu Chula', a clean cookstove designed for an efficient burn to reduce fuel use, helping to support higher air quality.
- The creation and protection of a 120,000-hectare conservation reserve in Brazil, aiming to reduce deforestation and assisting with employment opportunities for local communities in forest conservation and monitoring.

Notes:

1. Scope 1 and 2 emissions.
2. 2022 and 2021 average number of employees for the year available on page 217.
3. The 2021 result of 3.4 and the 2019 result of 5.4 differ from the previously reported results on page 73 of the Group's 2021 Annual Report and Accounts, following the validation of our Science-Based Targets (also see footnote 1 and 2 on page 69).
4. Prior to 2019, the emissions used in the calculation of the intensity metric excluded emissions from additional vehicles used during repairs, courtesy car fuel usage and vehicles that are Company funded, as these were not previously tracked.

External ratings, memberships and benchmarks

We actively support a variety of membership organisations, and disclose information to ratings and benchmarking authorities, as well as receive ESG performance ratings.

MCSI

We maintained an 'AA' rating for activity in 2022

Sustainalytics

As of October 2022, we received an ESG Risk Rating[1] of 18.2 and were assessed by Sustainalytics[2] to be at a low level of risk

Ecovadis

We were awarded a Silver medal in 2022

Carbon Disclosure Project

We achieved a C rating, ahead of our Science-Based Targets being approved

Science-Based Targets

We became one of the first personal lines insurers in the UK to have carbon reduction plans approved by the SBTi

Race to Zero

As a Race to Zero pledge, we've signed the Business Ambition for 1.5°C future aligning with our Science-Based Targets being approved this year

Get Nature Positive

We are a supporter of the Get Nature Positive campaign, focused on restoring nature and biodiversity

Social Mobility Pledge

We support the Social Mobility Pledge and have focused on helping students with their careers through our Community Fund

Women in Finance

We are a signatory to HM Treasury's Women in Finance Charter

Race at Work Charter

We support the Race at Work charter to take positive action towards supporting ethnic minority representation and inclusion

The Faith & Belief Forum

We are a signatory of the Charter for Faith & Belief Inclusion which aims to help create understanding between people of different faiths and beliefs and a society which is fair to people of all backgrounds – religious and non-religious

Notes:
1. Assessed to be at a low level of risk of experiencing material financial impacts from ESG factors.
2. Copyright © 2022 Morningstar Sustainalytics. All rights reserved. This section contains information developed by Sustainalytics (www.sustainalytics.com). Such information and data are proprietary of Sustainalytics and/or its third-party suppliers (Third Party Data) and are provided for informational purposes only. They do not constitute an endorsement of any product or project, nor an investment advice and are not warranted to be complete, timely, accurate or suitable for a particular purpose. Their use is subject to conditions available at https://www.sustainalytics.com/legal-disclaimers

Task Force on Climate-related Financial Disclosures

Introduction

Our 2022 disclosure against the recommendations of the Task Force on Climate-related Financial Disclosures ("**TCFD**") reports on our progress to date and outlines the actions we are taking to strengthen our strategic response to climate change.

The Group, as at the time of publication, has complied with the requirements of Listing Rule 9.8.6R by including climate-related financial disclosures consistent with 9 of the 11 TCFD Recommendations and Recommended Disclosures for all sectors including the supplemental guidance for insurance companies. The Group has reported against all 11 recommended disclosures and believes its disclosure against 9 of the 11 recommendations meets the objectives of the TCFD framework, with the two outstanding recommendations explained below.

For metrics and targets disclosure recommendations (a) and (b) of the TCFD framework, we aim to explore further how we strengthen alignment to the following specific components of these recommendations in future reporting. We aim to:

- explore how we incorporate additional metrics within our disclosure, including cross-industry metrics as recommended by the TCFD, to support measurement and management of transition risks and opportunities;
- assess disclosure of the extent to which our insurance underwriting activities, where relevant, are aligned with a well below 2°C scenario; and
- assess disclosure, where data and methodologies allow, the weighted average carbon intensity or GHG emissions associated with commercial property and specialty lines of business.

Governance

Our approach

The Group's approach to the governance of its sustainability strategy is underpinned by our Vision and Purpose (see page 10) and a clear commitment from the Board and senior management to align sustainability goals with the Group's strategy, and encourage accountability across the business.

Our five-pillar sustainability strategy, endorsed by the Board, aims to foster the highest standard of Environmental, Social and Governance practice and deliver long-term sustainability for all our stakeholders. The Planet pillar takes the lead on climate-related issues and is sponsored by our Chief Risk Officer ("**CRO**").

Boards and Committees

The potential impact of climate change on the business ("**inbound**"), as well as the Group's impact on the environment ("**outbound**"), are issues requiring robust governance to empower business areas in the management of climate-related risks and opportunities.

It starts with the Group's Board, which seeks to underpin all of the Group's activities with the highest standards of corporate governance. The Board has oversight on two key aspects of the Group's approach:

- Each year, the Board assesses the strategic plan (the "**Plan**") in conjunction with the Group's Own Risk and Solvency Assessment ("**ORSA**"), which considers material risks to the Plan, including climate change-related risks.

Highlights in the year

- **Received approval of our carbon reduction plans**, confirming that our emissions reduction targets are in line with a 1.5°C pathway, making us one of the first personal lines general insurers in the UK to gain approval by the Science Based Targets initiative ("**SBTi**").
- **Expanded our electric vehicle insurance package**, which is now offered to all Direct Line Motor customers to support the transition to a low-carbon economy and make it easier for customers to insure electric vehicles.
- **Incorporated a climate-related measure in our LTIP**, which now includes a measure of performance against our approved science-based emissions reduction targets.

- The Board oversees the Group's sustainability activity through its Committees, which scrutinise and provide appropriate challenge on the Group's five pillar sustainability strategy, including the establishment and monitoring of Science-Based Targets and the Group's participation in the Bank of England's Climate Biennial Exploratory Scenario ("**CBES**"). The Chair of each Committee reports to the Board after each Committee meeting.

Committees

- The **Audit Committee** meets a minimum of four times a year and is responsible for overseeing the Group's financial statements and non-financial disclosures, including climate-related financial disclosures.
- The **Board Risk Committee** oversees all aspects of financial, regulatory and operational risk, including the long-term risk to the Group from climate change. It meets a minimum of four times a year and receives reports on stress testing of long-term climate change scenarios, discusses strategies for managing the associated risks and considers emerging risks at least twice a year. The Committee played a key role in reviewing and challenging the actions and responses to the Bank of England's CBES exercise.
- The **Investment Committee** meets a minimum of three times a year and considers the strategy for incorporating ESG factors into the Group's investment management, which has seen our credit portfolios tilted to issuers with higher sustainability weightings.
- The **Nomination and Governance Committee** meets a minimum of two times a year, monitoring the Board's overall structure, size, composition and balance of skills. This Committee is also responsible for monitoring the Group's observance of corporate governance best practice.
- The **Sustainability Committee** scrutinises progress against the sustainability strategy to ensure that we continue to make progress under our Customer, People, Society, Planet and Governance pillars. The Committee meets a minimum of four times a year and has overseen: the setting of the Group's Science-Based Targets; activity undertaken by the Group to move towards becoming a net zero business; and Group involvement in climate debates, including the ABI's Climate Change Roadmap, the Partnership for Accounting Financials' methodology for underwriting emissions disclosures

and the Sustainable Markets Initiative Insurance Task Force. During the year, the Committee has discussed prominent public policy challenges such as flooding and accelerating the transition to electric vehicles. From 2023, the Committee will also receive biannual updates on the Group's performance against its science-based emissions reduction targets, following their approval by the SBTi in 2022.
- The **Remuneration Committee** meets a minimum of four times a year and considers how executive remuneration can be used to drive progress on climate related matters. It has introduced an emissions measure in our LTIP based on the greenhouse gas reduction targets approved by the SBTi.

More information on the structure of the Board and Board Committees can be found within the Corporate Governance report on page 110.

Management's role

There are three primary management roles designed to assign responsibility for the delivery of the Group's assessment and management of climate-related matters:

- the acting CEO has overall responsibility for climate change and environmental matters;
- the CRO is responsible for overseeing the management of climate change-related risk, and sponsors the Planet pillar of the Group's sustainability framework. The CRO is also the senior manager with responsibility for assessing and monitoring climate change-related financial risk. In that capacity, the CRO oversees the work of the Risk Function in analysing and stress testing the potential future impact of climate change on the business. The results of these stress tests are submitted to the Risk Management Committee, the Board Risk Committee and the Board, including as part of the ORSA; and
- the CFO is responsible for overseeing the implementation of the Group's investment strategy and is advised by the Investment Committee on the application of ESG weightings, including those related to climate change, to the relevant portfolios. The CFO is a member of the Investment Committee and the CRO and the Director of Investment and Capital Management are attendees.

To support the Sustainability Committee's oversight, and in recognition of the Group's increased focus on climate-related activity, the Group formed a **Climate Executive Steering Group** which reports into the Sustainability Committee. Chaired, in the year, by Tim Harris, our former CFO, the Climate Executive Steering Group consists of members representing various teams from across the business to assess potential impacts of climate change with the aim of ensuring risks are identified and managed effectively. The Steering Group's responsibilities include:

- monitoring and driving performance against the Group's Science-Based Targets;
- overseeing input in the Group's business development and strategic processes to make sure climate is given appropriate consideration in long-term strategy and planning; and
- considering the risk management challenges presented by climate change, including financial risk related to underwriting and investments.

Note:
1. Ongoing operations – see footnote 1 on page 25.

Further information relating to our risk identification process and the processes by which management are informed about climate-related issues can be found on page 81.

Group Audit

Group Audit provides an independent and objective view of the adequacy and effectiveness of the Group's risk management, governance and internal control framework. Group Audit are represented at the Climate Executive Steering Group.

Strategy

Climate change has far-reaching implications for economies and societies around the world. The physical and economic impacts that could result from further global warming may be significant and the extent of these impacts is dependent on the action taken to tackle climate change.

As a major UK insurer with over 9.6 million in-force policies from ongoing operations[1] we have a role to play in supporting the transition to a low carbon economy and we know that through our actions as a business we can contribute to climate risk mitigation.

The following pages examine the potential impacts of climate change on our business, in line with the TCFD recommendations, and outline the actions we are taking to strengthen our strategic response to one of the biggest challenges facing the world today.

Climate change risks and opportunities

The potential impacts of climate change on organisations are classified into the following three categories by the TCFD:

- **physical risks –** resulting from the physical effects of climate change;
- **transition risks –** resulting from the transition to a lower-carbon economy; and
- **opportunities –** arising from efforts to mitigate and adapt to climate change.

We also recognise that litigation risks, which includes risks arising when parties who have suffered losses from climate change seek to recover them from those they believe may have been responsible, could also cause adverse impact. This could include direct climate-related litigation against the Group or insurance risk arising from the underwriting of liability products, for example. The Group considers the risks associated with this to be low due to low exposure in high-risk industry sectors.

Materiality

We recognise that assessing and quantifying the level of impact from climate change is an emerging practice.

A greater level of estimation and assumption is required to address the long-term and forward-looking nature of climate-related risks and opportunities, which causes limitations in assessing materiality. Our intention is to explore further how we can enhance our approach to materiality, in the context of climate change, with more certainty.

More information on our current approach to measuring the impact of climate-related risk, and the integration of climate change in the Group's overall risk management processes, can be found on pages 74 and 81.

Defining the short-, medium- and long-term time horizons

Short	**1 – 10 years**
Medium	**10 – 30 years**
Long	**30 years +**

Our approach to defining the time horizons associated with climate-related risks and opportunities is to align closely with the scenarios considered in the Group's quantitative analysis of climate-related risk, which typically considers scenarios that span thirty years or longer (see page 75).

When defining the time horizons, the useful life of assets was considered. However, the Group's assets are primarily depreciated or amortised over a period of up to 10 years. As such, from a climate-related risk perspective, this falls into our short-term time horizon and therefore climate-related risk is not a significant input into determining asset useful economic lives.

The time horizons over which specific climate-related issues will manifest themselves vary significantly. However, in general, transition risks are likely to materialise more rapidly than physical risks, which are likely to be gradual and materialise over the longer term. The timing of climate-related litigation risk is less certain due to the nature of the exposure.

The key physical and transition risks and opportunities that could significantly impact the Group, as well as the time horizons over which they could manifest, is available further into our disclosure, see pages 78 to 81.

Financial planning, performance and position

Without appropriate management, the risks posed by climate change could adversely impact the Group's financial performance and financial position.

To help quantify the potential impact of climate change we:

- perform scenario analysis, which enhances our understanding of the financial risks associated with the longer-term impacts of climate change and provides an indication of strategic resilience (see pages 75 to 77);
- undertake climate risk modelling to assess the most predominant physical drivers of risk in our property insurance products, enabling us to evaluate the potential impact to the Group's capital position (see page 82); and
- integrate climate risk into the Group's overall approach to risk management. This includes measuring the relative significance of climate-related risks to other risks in the Group Risk Taxonomy (see page 81).

Financial planning

We have identified that limitations exist in aligning climate change and financial planning. A key issue relates to the modelling of climate change impact, which typically extends out to thirty or more years, a significantly longer period than our current financial plan.

Although limitations and uncertainties associated with the longer-term impacts of climate change exist, the prominence of climate-related considerations in our most recent planning continued to grow.

The Group's Plan reflects the strategic planning that is ongoing across the business and therefore covers any climate-related initiatives that are embedded within. These include:

- sustainability-related projects, such as the actions we are taking to reduce the carbon footprint of our accident repair centres and investment portfolio and the associated costs. More information on these actions can be found on page 80 and 81;
- the use of reinsurance in our property insurance business, acknowledging that the cost to obtain catastrophe reinsurance could be impacted by an increase in the frequency and severity of major weather events;
- development of propositions and channel expertise to support the transition to a low carbon economy, such as our electric vehicle offer, which is now available to all Direct Line Motor customers; and
- the reduction of our office footprint, seen, for example, through our planned move from our office site in Bromley to a smaller Central London hub in 2023.

We also monitor losses from major weather events, which include inland and coastal flooding, storm surge, freeze events and subsidence. We use sophisticated modelling techniques to determine the expected losses from major weather events in our Home and Commercial property book to set a weather load for budgeting purposes. The impact of major weather relative to this load for 2022 and prior years can be found on page 83.

Financial performance and position

In preparing the financial statements, the Group has assessed the impact of climate change. While the risks associated with climate change remain uncertain looking forwards, the impact of major weather events is reflected in the Group's historical performance and position as at 31 December 2022. The potential impact of climate change on insurance risk is also discussed in further detail within note 3 to the consolidated financial statements (see page 200).

Areas of physical and transition risks the Group could be exposed to are outlined in the table on page 78. The financial impact of these risks can, if realised, be grouped broadly into the following:

- Adverse impacts to revenue and market share due to a failure to understand the scale of change in market demand for products and services due to climate-related policy, technology and consumer preference.
- Increased climate-related operating costs and capital expenditure due to the investments we make to reduce our carbon footprint and to progress towards our long-term emission reduction commitments.
- Changes in the value of our financial investments due to the influence of physical and transition risk impacting the wider economy.
- An increase in the frequency and severity of natural catastrophes and other weather-related events adversely impacting insurance liabilities.

We also recognise that our access to capital can be materially affected by factors including, but not limited to, financial performance and investment decisions, which have their own associated climate-related risks. In addition, our performance is assessed externally by ESG rating agencies, to which investors and other stakeholders are giving increasing prominence. Adverse impacts to our debt rating could negatively affect cost and access to sources of debt finance and subsequent interest rates.

In our approach to acquisitions and divestments, any climate-related risks and opportunities are expected to form part of our usual due diligence process.

Scenario analysis

Our most recent scenario analysis activity took place during 2021, followed by a smaller round of analysis in early 2022.

The analysis was designed to enhance our management of climate-related financial risk and the scenarios used expanded on the Network for Greening the Financial System's ("**NGFS**") Net Zero 2050, Delayed Transition and Current Policies scenarios by including additional risk transmission channels and adding additional variables.

The exercise considered the financial impacts from these three distinct climate scenarios at a ten- and thirty-year time horizon, capturing a range of different combinations of transition and physical risks. Two of the scenarios represent routes to net zero greenhouse gas emissions and primarily explore transition risk from climate change:

- **Early Action** The transition to a net zero emissions economy started in 2021, so carbon taxes and other policies intensify relatively gradually over the scenario horizon. Global carbon dioxide emissions are reduced to net zero by around 2050. Global warming is limited to 1.8°C by the end of the scenario (relative to pre-industrial levels). Some sectors are more adversely affected by the transition than others, but the overall impact on GDP growth is muted, particularly in the latter half of the scenario, once a significant portion of the required transition has occurred and the productivity benefits of green technology begin to be realised.
- **Late Action** The implementation of policy to drive transition is delayed until 2031 and is then more sudden and substantial. Global warming is limited to 1.8°C by the end of the scenario (relative to pre-industrial levels). The more compressed nature of the transition results in material short-term macroeconomic disruption, which is particularly concentrated in carbon-intensive sectors. Output contracts sharply in the UK and international economies. The rapid sectoral adjustment associated with the sharp fall in GDP reduces employment and leads to some assets being stranded, with knock-on consequences for demand and spending. Risk premiums rise across multiple assets. An important indicator of the level of transition risks in these scenarios is the carbon price, reflecting that policymakers can induce the transition by increasing the implicit cost of emissions.

The third scenario primarily explores physical risks from climate change in the event that there are no new climate policies introduced beyond those already implemented:

- **No Additional Action** The absence of transition policies leads to a growing concentration of greenhouse gas emissions in the atmosphere and, as a result, global temperature levels continue to increase, reaching 3.3°C relative to pre-industrial levels by the end of the scenario. This leads to chronic changes in precipitation, ecosystems and sea level. UK and global GDP growth is permanently lower and macroeconomic uncertainty increases.

For each of the three scenarios, variable paths were provided for the underlying physical and transition risks and for mapping these risks onto macroeconomic and financial variables:

- Physical and transition risks: pathways for climate variables to represent the impact of climate risks and opportunities at the global and regional level.
- Macroeconomic and financial market conditions: impact of climate-related risks and opportunities at a global level, and at the level of key countries, regions, and sectors – reflecting the impacts of physical and transition variables in each scenario. Financial market conditions reflect the direct financial market consequences of the paths of the macroeconomic variables.

Our analysis focused on changes in invested assets and insurance liabilities, and the variables provided formed the basis for the modelling. The stress assumed an instantaneous shock, effectively bringing forward the future climatic environment to today's balance sheet, with no allowance for changes in future premiums, asset allocation, expenses, reinsurance programmes and other future changes in business models.

The analysis was applied to the Group's Solvency II balance sheet as at 31 December 2020 and assumed fixed balance sheets, premiums, exposures and reinsurance arrangements.

Summary of results

The results show the most material impact on the Group's Solvency II own funds arises in the No Additional Action Year 30 scenario, in which transition risk on the investment portfolio dominates the overall impact. These large impacts reflect the cumulative downward trend in asset values, with no stabilisation effects observed (unlike the other two scenarios) as extreme weather events increase in frequency and intensity, and continue to affect economic growth beyond the thirty-year horizon considered by the analysis.

The No Additional Action Year 30 scenario also shows the largest increases in insurance liabilities, in absolute terms, which is consistent with estimated increases in Gross Average Annual Losses ("**AAL**") of around 150% for inland flooding and around 370% for coastal flooding. This could result in a material increase in weather load, reinsurance costs and capital load. While the short-term nature of the business, the ability to re-price annually and the risk mitigation provided by reinsurance arrangements are likely to limit the impact on general insurance liabilities, the modelling has illustrated that the increased physical effects of climate change could potentially result in some risks and perils becoming either uninsurable or unaffordable.

Relative Impact – No Additional Action to Early Action

The following graph illustrates the potential adverse impact to the Group's Solvency II balance sheet value of investment assets and insurance liabilities at Year 30 under the Early Action, Late Action and No Additional Action scenarios.

The most adverse financial impact was from the No Additional Action scenario, which is set at 100% in the graph. When compared to the total impact under the No Additional Action scenario, the impact of the Late Action scenario was around 54% of the value and the impact under the Early Action scenario was around 39% of the value.

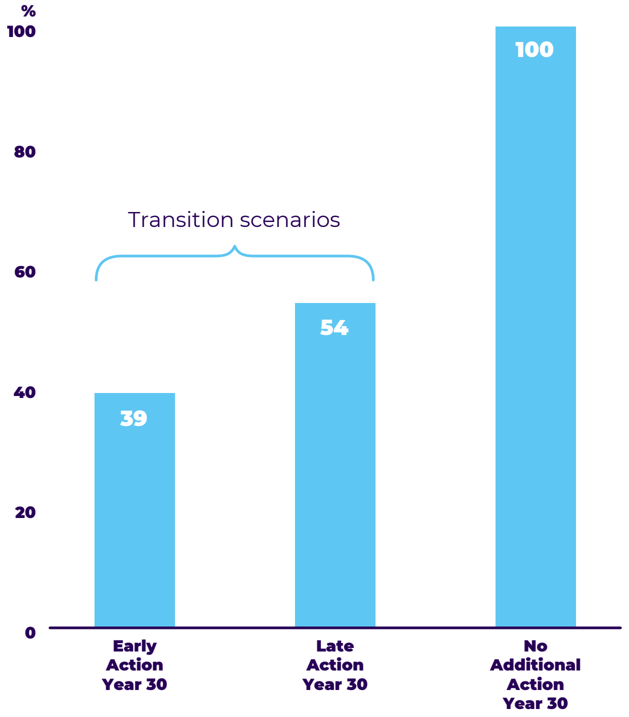


Figure 1: Year 30 impacts of scenarios relative to the largest No Additional Action scenario

In the Late Action scenario, the delay in policy implementation to transition to a low-carbon economy means there are no transition impacts over the initial ten-year time horizon. However, accelerated transition from 2031 results in greater impacts versus the Early Action scenario over the thirty-year time horizon. Whilst both of these transition scenarios saw material impacts on the investment portfolio, the most significant impacts on both investments and insurance liabilities arose from the physical risk effects of no transition in the No Additional Action scenario (where no additional actions are taken beyond those already announced).

At the thirty-year time horizon, financial impacts in the No Additional Action scenario are nearly double those in the Late Action scenario, and physical risks also drove the largest impact on investment results in absolute terms. However, these impacts do not take into account the Group's long-term commitments within its investment strategy, which includes the target of holding a net zero emissions investment portfolio by 2050 (see pages 80 and 84).

All three scenarios would lead to a breach in risk appetite, and the No Additional Action Year 30 scenario would also lead to a breach in SCR based on the Solvency II balance sheet as at year-end 2020. However, a set of clearly defined management actions could be deployed in each scenario to address the risks and allow the business to recover to above risk appetite (see page 77).

Comparison of impact – insurance liabilities and investments

The graph below shows the potential adverse impact on the Solvency II balance sheet value of investment assets and insurance liabilities under the Early Action, Late Action and No Additional Action scenarios at Year 10 and Year 30.

The graph outlines how the total impact for each scenario (set at 100%) is split between the impact on investments and insurance liabilities to illustrate their relative materiality. For example, in the No Additional Action Year 10 scenario, impacts are split broadly evenly, while in the corresponding Year 30 scenario, the impact on investments dominates.

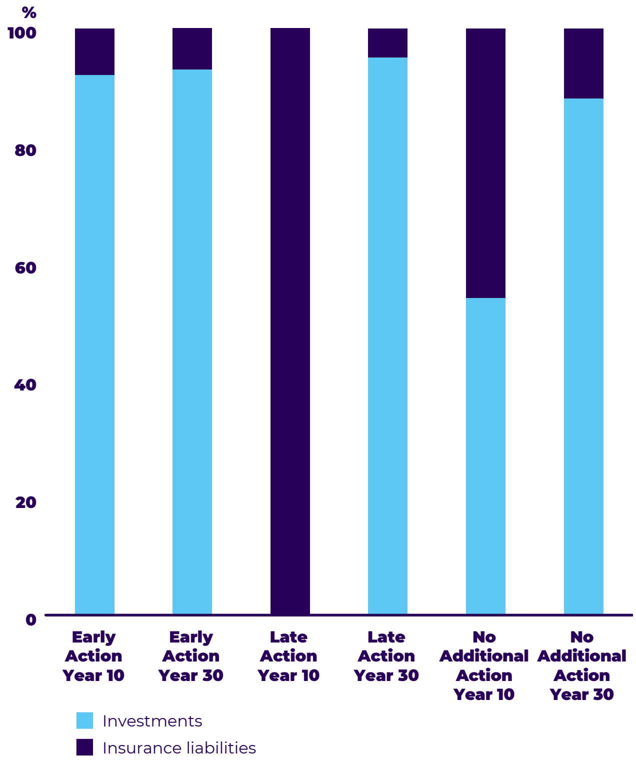


Figure 2: Share of impact – insurance liabilities and investments

Except in the Late Action Year 10 scenario, where there is no transition risk due to the assumed delay, in all scenarios the impact on investments is more material than on insurance liabilities. Additionally, insurance liabilities were considered gross of reinsurance and, in practice, factors such as the short-term nature of the business, the ability to re-price annually and the risk mitigation provided by reinsurance arrangements is likely to limit the impact on general insurance liabilities further.

Physical risk by peril

The following graph illustrates the potential adverse impact of physical risk on the Solvency II balance sheet value of insurance liabilities at Year 30 under the Early Action, Late Action and No Additional Action scenarios.

The total impact (set at 100%) is further analysed by peril, for example in the No Additional Action scenario around 60% of the total impact is driven by inland flooding and 33% by coastal flooding.

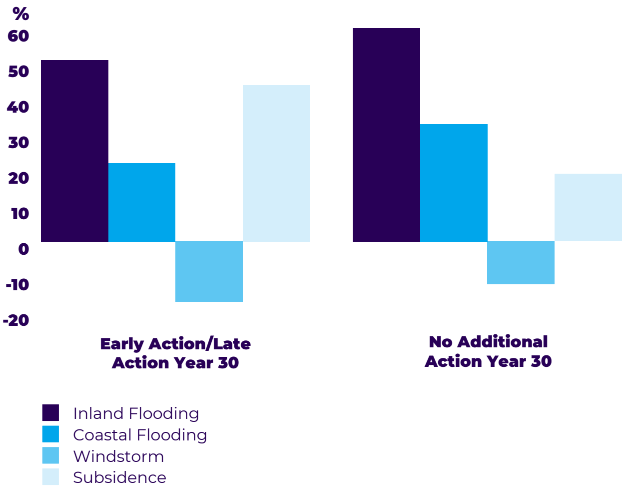


Figure 3: Split of physical risk impacts on insurance liabilities by peril

Figure 3 shows that, on a gross basis, the physical risk to insurance liabilities across all three scenarios was largely driven by inland flooding and coastal flooding, which included storm surge due to a rise in sea levels. However, the analysis shows that the changes to flood and storm surge risk vary regionally. Windstorm was assessed to have a small positive benefit over all scenarios as a result of changing atmospheric conditions driven by complex interactions of a number of variables, ultimately caused by rising temperatures.

Management actions

Undertaking this analysis provided us with a framework to identify and assess the climate-related transition and physical risks that the business could be exposed to.

Taking into account the level of impacts that we have observed as part of this climate-related modelling, we identified a number of management actions that would be effective to mitigate these risks and respond to new opportunities.

Our Management Action Framework consists of three broad categories based on the purpose and nature of the action:

- **Contingent Management Actions –** These follow the Group's existing Contingent Management Actions framework and would be deployed to mitigate the scenario impacts, assuming these arise as instantaneous shocks on the balance-sheet; potential action could include restricting capital distributions, for example.
- **Pre-emptive Management Actions –** These have been developed assuming that the business can observe the scenarios unfolding in real time and begin to adapt the business model in response to these emerging impacts; they cover areas such as repricing, de-risking of investments and reinsurance.
- **Strategic Management Actions –** These actions are aligned to the Group's ongoing strategic activity as part of our contribution to the transition to a lower-carbon economy. They include: taking action to progress against our net zero ambitions and Science-Based Targets; understanding how we can support in improving the flood resilience of UK properties in flood-prone areas; and evaluating the impact of climate change on our underwriting footprint. Progress against these actions is overseen by the Climate Executive Steering Group. For further information on our Strategic Management Actions, see page 65.

CBES second round

In early 2022, we participated in the second round of the Bank of England's CBES exercise. The initial CBES exercise, that took place in 2021, was designed to test the resilience of the UK financial system to physical and transition risk from climate change to assist banks and insurers in enhancing their management of climate-related financial risk.

For general insurers the second round focused on management responses to the CBES scenarios and resulting challenges to the business models. More specifically, it probed how responses would change if losses were higher; encouraged additional thinking about dependencies and actions required by the government and other associated stakeholders; and further explored opportunities in the climate scenarios.

In response, the Group concluded that the climate-related management actions identified in the initial analysis would remain appropriate. However, the pre-emptive management actions of repricing and reinsurance, as well as the strategic management actions relating to flood resilience and underwriting footprint, would be accelerated after considering a scenario under which physical losses from climate change were materially higher.

The second round of analysis was based on the modelling outputs from the initial exercise, as in the short term re-running the CBES scenarios is unlikely to produce materially different results.

Going forward, we will continue to work towards developing scenarios specific to our own risk profile that focus on the most material aspects of our business and explore the sensitivity of potential impacts to key uncertainties. This will enable the Group to make use of scenario-testing output more effectively to further inform our strategic approach to mitigating climate-related impacts.

Our strategic response

In order to ensure strategic resilience, we must manage the exposure against the potential risks from climate change and harness opportunities from the transition to a low-carbon economy. Our strategy focuses on driving change across three key areas of the business: our underwriting activities, which includes a focus on the operating segments that could be most affected by climate change; our operations; and our approach to investments. These are considered in turn on pages 79 to 81.

The following table outlines key physical and transition risks and opportunities that could significantly impact these areas as well as the time horizons over which they could manifest. Our definition of the time horizons can be found on page 74.

Category	Description	Examples of potential impact on the Group	Time horizon	Key area of impact
Physical risks	**Acute** – event driven risks such as flooding and storm surge. **Chronic** – longer-term shifts in climate patterns, such as a continued rise in average temperatures, changes in, and extreme variability of, precipitation and weather patterns and rising sea levels.	An increase in the frequency and severity of natural catastrophes and other weather-related events could adversely impact insurance liabilities.	S	U
		Disruption to our direct operations, which could include damage to our estate, impacting our ability to serve customers.	S M L	O
		Chronic risks could lead to significant changes in our underwriting criteria to maintain risk appetite, and/or higher costs to obtain catastrophe reinsurance to protect us against an accumulation of claims arising from a natural perils event.	M L	U
		Reduced returns from investments in companies whose operations are impacted by physical climate risks, and real asset investments directly impacted by physical climate risks.	S M L	I
Transition risks	Risks arising from the transition to a lower-carbon economy. These are categorised by the TCFD as: – policy and legal risks; – technology risks; – market risks; and – reputational risks.	A failure to understand the scale of change in market demand for products and services due to climate-related policy, technology and consumer preference could impact revenue and market share.	S M	U O
		Costs associated with the transition to a lower-carbon economy may increase over time and the adoption of new lower emissions technologies may be unsuccessful.	S M	O
		Insufficient progress against our net zero ambitions could cause stakeholder concern and reputational damage.	S M L	U I O
		Reduced returns from investments in high carbon intensity companies that are not taking action to transition to a low carbon economy, and real asset investments that are not compatible with the transition to a low carbon economy.	S M L	I
Opportunities	Efforts to mitigate and adapt to climate change can also produce commercial opportunities. These could allow us to help accelerate the transition and continue contributing to a sustainable economy.	Accelerating the speed of transition to a lower-carbon economy by, for example, supporting the move to greener transport solutions, particularly electric-powered cars, allows us to develop new insights and capabilities to help us build insurance solutions that best meet our customers' evolving needs.	S M	U
		Investment in energy-efficient features and equipment across our office estate and accident repair centres could save on energy consumption and operating costs, reduce our footprint and improve operational and resource efficiencies.	S M L	O
		Potentially enhance risk-adjusted returns from our investments by aligning the investment portfolio with the transition to a low carbon economy whilst also enhancing our reputation as a responsible investor. Ensuring the investment portfolio is resilient against the physical effects of climate change.	S M L	I

Key

S Short-term M Medium-term L Long-term
U Underwriting I Investments O Operations

Underwriting

Property
The physical risks from climate change are most likely to manifest themselves as an insurance risk on our property insurance products.

Recent weather events that we have responded to highlight the importance of, and need for, insurance. In December, the prolonged period of sub-zero temperatures saw us help thousands of customers deal with burst pipes and water tanks and other related damage. The record-breaking temperatures experienced across the UK in Q3 led to a modest increase in subsidence claims in our Home business, and in early 2022, we supported our Home and Commercial customers following three significant storms: Dudley, Eunice and Franklin.

The frequency and severity of natural catastrophes and other weather-related events in the UK are key drivers in the Group's solvency capital requirements. The short-term nature of the business we underwrite, the ability to re-price annually, and the risk mitigation provided by reinsurance arrangements are important factors in how we manage our exposure.

However, acknowledging that, in general, the physical risks from climate change are likely to intensify over the longer-term, there remains a need to assess how this risk could impact the Group over a significantly longer period.

To support our assessment of the potential impact on insurance liabilities over the longer-term we undertake scenario analysis (see pages 75 to 77). The analysis helps us to quantify the financial implications of physical risk under different possible future climate scenarios. The outputs provide an indication of the Group's resilience and aid our strategic planning.

The outcomes of our most recent scenario analysis provided a framework to identify and assess climate-related risk and develop a set of contingent and pre-emptive management actions (page 77). The analysis also supported the development of our Strategic Management Actions which span across business areas and include action on:

- engaging with policymakers on the importance of flood defences in the UK to protect properties located in flood-prone areas;
- exploring how we can help shape the thinking around resilient repairs of properties affected by flooding; and
- further evaluating the impact of climate change on our underwriting footprint and risk appetite.

For more information on our Strategic Management Actions see page 65.

Motor
As one of the largest motor insurers in the UK, the move to electric-powered vehicles is particularly pertinent. Supported by changes in technology and policy, such as Government plans to end the sale of new petrol and diesel cars in the UK by 2030, the speed of transition to electric continues to increase.

The transition to a low carbon economy presents new challenges, but also new opportunities. As part of our response, we are developing further insight into the future of vehicle technology and repair, growing our data and developing 'green' products to support our customers who are already making the switch to electric.

To date, our actions include:

- developing a full electric vehicle package which is offered to all new and renewing Direct Line Motor customers that provides access to electric vehicle essentials, discounts off our Green Flag Shop and insurance that covers batteries and charging cables (see page 67);
- establishing a dedicated Electric Vehicle Distribution and Strategy team, focused on evolving the Group's strategic response to the electric shift; and
- entering into new strategic partnerships, such as our new partnership with Motability Operations from September 2023, where we expect the number of electric vehicles we insure to grow significantly over the course of the ten-year partnership.

Operations
Operating in a sustainable way is key to minimising our impact on the environment. Taking action to reduce our carbon footprint is also good for the sustainability of our business, and an important part of how we can mitigate against potential climate risks that could cause disruption to our operations.

Science-Based Targets
We previously disclosed our aim to achieve net zero emissions by 2050 at the latest and to support our ambition, we announced we were setting Science-Based Targets.

In 2022, these targets were formally approved by the SBTi. This significant milestone in our carbon reduction strategy defines the path of how we reduce our carbon emissions further and underpins how we progress towards our ambition of becoming a net zero business.

The targets include an operational emissions target. This covers the Scope 1 and 2 GHG emissions generated from our direct operations, where we are aiming for a 46% reduction in absolute Scope 1 and 2 emissions from our office estate and accident repair centres by 2030, from a 2019 baseline.

More information on our Science-Based Targets can be found on page 66.

Although our journey to net zero emissions continues to gain momentum, we acknowledge that it will take time to facilitate the transition, which is why we continue to offset the carbon emissions[1] from our operations we cannot yet avoid (see pages 65 and 70).

We calculate and report our GHG emissions annually. Our most recent carbon emissions reporting can be found on page 69 and further disclosure on the progress we have made in reducing our footprint to date can be found on page 84.

With a history of taking action to reduce our environmental impact, we are well placed to drive down our emissions further.

In recent years we have taken steps to understand where the most carbon-intensive areas of our operations are. One area where we are prioritising our carbon reduction activity is across our accident repair centres.

Fundamental to serving our motor insurance customers, our 22 accident repair centres are embedding a range of solutions as part of our carbon reduction strategy led by colleagues in our Auto Services Sustainability Programme.

In support of our operational Science-Based Target (see page 66), action taken this year has included:

- expanding the use of hydrogenated vegetable oil in our accident repair centres as an alternative fuel for our recovery trucks, resulting in 543 tonnes of CO_2e saved in 2022;
- fitting energy-saving LED lighting to a further six repair centres meaning nearly 70% of our Auto Services sites have now received these upgrades;
- installing a Power Factor Corrector in our Birmingham Auto Services site to maximise the efficiency of our electrical supply on-site. In 2021, installation at our Crawley repair centre delivered a 13% improvement in energy efficiency. We are exploring expanding this to include installation at more repair centres in 2023; and
- further exploring the feasibility of moving from gas powered paint booths to electric.

We are also reducing our office footprint which includes moving our head office from Bromley to a newer smaller Central London property in 2023.

Supply chain

Our Sustainable Sourcing Approach, launched in 2021, aims to reduce the emissions in our supply chain. Our approach means we are engaging with our largest emitting suppliers to encourage them to sign up to SBTi targets or an equivalent. We are also requesting information on what efforts firms have made to measure their carbon footprint across Scopes 1, 2 and 3 and their plans to reduce emissions so we can evaluate whether it is viable to change our sourcing approach on appropriate contracts.

In 2022 we also set an internal emissions reduction target (see page 66) and we report the GHG emissions from our supply chain annually, these can be found on page 69.

Investments

In recent years, we have begun integrating more ESG considerations into our investment strategy, recognising this is a long-term process which will require assessment and challenge to inform future decision making.

We know that the impacts of potential physical and transition climate-related risks arising in the wider economy will have an impact on our investment portfolio, through their influence on the value of assets. For example, our portfolio is exposed to physical risks through our investment in companies that are exposed to disruption from adverse weather events across their supply chain. It is also exposed to transition risks, where companies that we are invested in are not adapting their strategy to a low-carbon future. However, the transition to a low-carbon economy also creates significant investment opportunities.

We have the long term goal of our entire investment portfolio being net zero emissions by 2050 and in support of our aims we continue to implement key climate initiatives into our investment strategy. During 2022, we:

- received approval from the SBTi for our science-based GHG emission reduction targets in our investment portfolio (see below);
- became a signatory to the CDP's science-based targets campaign; a collective engagement campaign supported by over 300 financial institutions with over $73 trillion in assets which encourages high emitters to set science-based emissions reduction targets; and
- continued to reduce the carbon intensity of our corporate bond portfolio in line with our aim of a 50% reduction by 2030 from a 2020 base year.

Science-Based Targets

In support of our long-term goal of ensuring our entire investment portfolio is net zero emissions by 2050, in line with the aims of the Race to Zero campaign, we set four science-based GHG emission reduction targets in our investment portfolio.

In 2022, we received formal approval of these targets from the SBTi. The targets cover corporate bonds, commercial real estate and commercial real estate loans which, as at the end of 2022, covered 63% of AUM. More information on the targets can be found on page 66.

The actions detailed above form part of the ongoing development of the wider ESG framework underpinning investments. In terms of holding investments in other companies, those with higher reported ESG credentials have more sustainable practices which better align to our investment, environmental and social goals. As such, a requirement of all investment-grade corporate bond portfolios is that each portfolio must maintain a minimum MSCI ESG rating of 'A' or better.

Note:
1. Scope 1 and 2 emissions as well as elements of our Scope 3 emissions under our direct control (see page 69).

Looking through the climate lens, we also have in place the following current initiatives:

- Thermal coal screen whereby we restrict investment in firms generating more than 5% of revenues from either thermal coal mining or thermal coal power production unless the company is taking positive climate action[1].
- We actively encourage our investment managers to invest in green bonds. Green bonds are designated bonds intended to encourage sustainability and to support climate-related or other environmental projects. All our relevant corporate bond mandate guidelines now direct the portfolio manager to purchase a green bond where the risk return characteristics are similar to those of a comparable non-green bond.
- Within our investment property portfolio all assets must have an Energy Performance Certificate of 'D' or better, or a plan and funds in place to achieve that level. The property portfolio also has a tailored set of ESG targets covering areas such as carbon, energy, water and waste.

Using our influence

We are committed to using our influence to drive wider change. For example, we expect all of our investment managers to be signed up to the UN Principles for Responsible Investment. We also talk regularly to our external asset managers to understand (and where necessary, challenge) how they are using their global presence, size and leverage to engage and encourage corporations to tackle climate change. This year we have also signed up to the CDP's science-based targets collective engagement campaign which encourages high emitters to set science-based emissions reduction targets.

Risk Management

Enterprise Risk Management Strategy and Framework

The Enterprise Risk Management Strategy and Framework sets out, at a high level, the Group's approach to setting risk strategy and managing risks to the strategic objectives and day-to-day operations of the business. Further information can be found in the Risk management section of the Strategic report on page 87.

Risk taxonomy

The effects of climate change are wide-ranging, affecting many risks across the risk universe. To allow for better recognition of internal and external drivers of climate-related risk and to provide a focal point for the reporting of risks relating to climate change, the Strategic Risk category has been broadened to include Climate Risk within Environmental, Social and Governance Risk.

Risk impact

The impacts of all risks, events and action plans are rated using the Impact Classification Matrix which facilitates a consistent approach to the sizing and categorisation of risk across the Group by using Financial, Customer, Reputation and expert judgement inputs. This includes those risks relating to climate change, including climate-related litigation risks, and allows the Group to determine the relative significance of climate-related risks in relation to other risks.

Climate-related risk identification process

Annual risk identification process

Each year, the business is required to review all current and developing risks which could impact on the achievement of strategic objectives. This process includes assessing risk drivers, such as those due to climate change, and their potential impact and likelihood of risk crystallisation on both an inherent and residual basis, in addition to identifying the position which aligns with risk appetite.

We also use a variety of indicators across our product segments to assess, monitor and manage climate-related risks. A number of these key metrics can be found on pages 82 and 83.

Regulatory monitoring

The Group monitors and reviews relevant outputs from the FCA, the PRA, and His Majesty's Treasury, to consider existing and emerging regulatory requirements.

During 2022, this included reviewing:

- the findings from the PRA's 2021 Climate Biennial Exploratory Scenario on financial risks from climate change;
- the Bank of England's letter from Sam Woods on the PRA's supervision of climate-related financial risk; and
- the minutes of the PRA and FCA's joint Climate Financial Risk Forum.

We continue to monitor future developments. Reviews are summarised and distributed to relevant stakeholders, and, where necessary, responses are co-ordinated and overseen by members of Second Line of Defence.

Emerging risk process

In addition to the annual risk review process, the Group has in place an emerging risks process which facilitates the identification, management and monitoring of new or developing risks which are difficult to quantify or are highly uncertain. The Group records emerging risks within an Emerging Risk Register. Updates on emerging risk and the actions being taken to address them are presented to the Risk Management Committee and the Board Risk Committee regularly, supplemented by deep dives on selected emerging risks. Each emerging risk is owned by an Executive sponsor to help ensure alignment of how it is managed to the strategic objectives and priorities; as well as a senior business leader who is responsible for day-to-day management of the risk.

Climate change is one of the Group's most prominent emerging risks, with regular oversight provided by the Climate Executive Steering Group, consisting of First Line of Defence subject matter experts from around the business where the impact of climate change is the highest, in addition to Second Line of Defence subject matter experts who provide oversight and challenge of risk management activity relating to this.

Both physical and transition risks could manifest themselves through a range of existing financial and non-financial risks, including insurance, market, operational and strategic risks. For more information on emerging risk and climate change see page 91.

Note:

1. Companies taking positive climate action are defined as those that are committed to setting Science-Based Targets or have a 2°C or better carbon performance alignment from the transition pathway initiative.

Climate risk modelling

The predominant direct physical drivers of risk to the Group's capital position are major UK floods and windstorms and these are modelled together with less material perils such as freeze and subsidence within the Group's Internal Economic Capital Model and reviewed at least biennially.

The influence of climate change is difficult to isolate from the complex oceanic and atmospheric processes driving UK weather. The Group uses catastrophe models to capture these factors, and in turn these models are regularly reviewed against specific criteria including how they have considered latest scientific thinking, to ensure they appropriately capture the Group's risk profile. Responsibility for this work sits within the Capital Management function.

The majority of our policies renew annually and are priced according to risk. Pricing algorithms use sophisticated rating engines to account for recent trends and are supplemented with views of catastrophic risk to seek to ensure sufficient pricing. These prices will evolve as climate change influences manifest themselves through changing loss patterns, and views of catastrophic risk develop because of rising sea levels, changes in precipitation rates and urban resilience.

Risk pricing models are built using historical data covering a multi-decadal time period for perils most likely to be influenced by climate change. This allows us to understand and incorporate long-term signals and past trends into our modelling. These models benefit from considerable amounts of internal and externally purchased data. External data is reviewed and updated regularly, and we maintain a relationship with data suppliers to understand the methodologies and assumptions in their work. Nevertheless, the underlying trends can be difficult to measure as they emerge through infrequent one-off catastrophe events and may have additional contributory factors (for example, deforestation increasing the pace of rainwater run-off upstream of a flood). Furthermore, future trends are likely to differ from past projections. As such, we recognise a range of uncertainty as to current and future impacts.

Increases in frequency and severity of large catastrophe weather events are mitigated by the Group's use of catastrophe excess of loss reinsurance. This reinsurance covers property (Personal Lines and Commercial) and Motor physical damage losses; in addition to significant capital benefits, it transfers the volatility of low-frequency, high-severity natural peril events away from the Group. The reinsurance purchase decision is a combination of catastrophe modelling, capital analysis, the Group's risk appetite, cost of cover and the overall income statement impact. Cover is typically purchased with an upper limit equivalent to a 200-year modelled loss and the retention will be based upon the amount that the Group is willing to sustain from such a loss. In addition, we purchase risk covers to protect against large individual commercial losses and we make extensive use of Flood Re to cede high flood risk residential properties.

Metrics and Targets

We use a variety of indicators across the different lines of our business to assess, monitor and manage our climate-related risks and opportunities.

The following pages focus on the metrics and targets we use across the three key areas of activity, as identified earlier in our disclosure: our underwriting activities; our operations; and our approach to investments.

Remuneration

We have now formally introduced a climate-related metric for our LTIP. This incorporates a carbon emissions measure based on our carbon emissions reduction targets that were approved by the SBTi in 2022. More information can be found in the Directors' Remuneration Report on page 141.

Our aim is to explore how we incorporate additional metrics, including cross-industry metrics as recommended by the TCFD, to support measurement and management of transition risks and opportunities in future reporting.

Underwriting

Weather-related loss impact

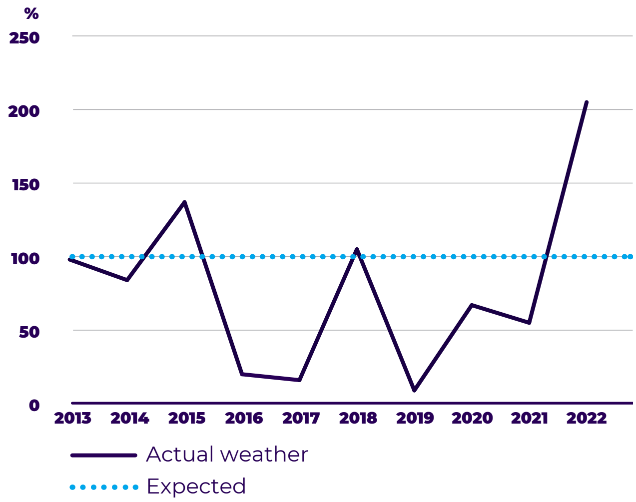
The predominant direct physical drivers of catastrophe weather risk from a capital perspective are major UK floods and windstorms. The last peak of windstorm activity was in the late 1980s and early 1990s; the last decade being particularly benign in comparison. By contrast, flood has seen more elevated activity.

Catastrophe reinsurance is purchased annually to protect against event losses greater than £150 million and additional reinsurance cover protects against large individual commercial losses (see page 37). Use of the Flood Re scheme mitigates against the highest individual residential flood risks.

The Group uses sophisticated modelling techniques to determine the expected losses from severe weather events and uses these to set a weather load for budgeting purposes.

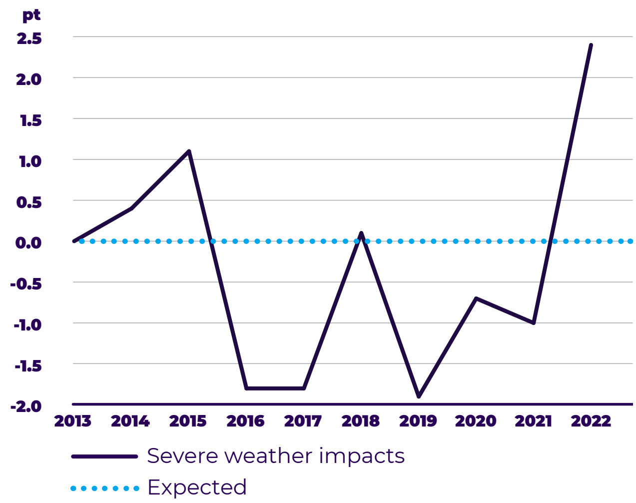
The following graph shows the impact of severe weather events relative to the weather load. In 2022, claims associated with severe weather exceeded our 2022 severe weather assumption, which is set at 100% in the graph.

Severe weather claims (actual % of expected loss)



Both these graphs reflect the number of major weather events in the year that the Group responded to, including three significant storms in Q1, a rise in subsidence claims from extremely high temperatures in the summer and the December freeze event.

Impact of severe weather on combined operating ratio[1] (pt)



Prior to 2022 the trends are reflective of relatively benign activity, although there is significant variability as shown in the graph. The 2018 peak was driven by the 'Beast from the East' freeze event whilst the 2015 peak was a result of a number of weather events in December which caused severe flooding across the UK.

The frequency and severity of extreme weather events will be affected by climate change, which in turn will affect our view of risk, how we price severe weather risk, and the type and level of reinsurance we purchase to protect our balance sheet.

Home

Key risk indicators are produced by the Underwriting function and reviewed quarterly through relevant business forums. The key climate change-related activities are flood, subsidence and other weather incidents. For flood and subsidence perils, we monitor the Group's market share for risks deemed to be in the high- or very high-risk segments. We also monitor and review the proportion of policies ceded to Flood Re. Each peril is monitored against set tolerances, with movements in amber or red ratings generating investigation and action as required. We maintain a view of trends and look to take action where a trend is likely to result in a breach of tolerance.

Flooding

Governments have been working with insurers since 2000 to help make flood risk insurance more affordable and in 2016 Flood Re was introduced. Every insurer that offers home insurance in the UK, the Group included, must pay into the Flood Re scheme. This levy raises around £135 million every year which is used to cover the flood risks in home insurance policies.

To ensure the Group and its customers benefit from the levy and guard against the highest of flood risks, we monitor the volume and proportion of policies we are ceding to Flood Re. Properties are eligible to be ceded to Flood Re when they meet certain criteria. Since early 2019, the cost to cede policies to Flood Re has dropped, driving an increase in ceded volumes.

Subsidence

We monitor this risk via our subsidence market share by geo risk classification. This risk classification aims to give a market view of geographic risk of having a subsidence claim. This enables us to understand the proportion of subsidence risk that we write compared to our estimate of the total in the market.

Motor

The Group's motor market is diversified throughout the UK, and although weather-related factors will influence claims frequency it is a relatively small influence compared with other factors, for example used car prices. As such we do not currently consider there to be any valuable climate-related risk indicators that can be tracked for this portfolio.

In order to track the transition towards electric and alternatively fuelled vehicles (such as hybrids), we monitor both the number and proportion of policies we underwrite for these types of vehicles as well as electric vehicle and alternatively fuelled vehicle registration data from The Society of Motor Manufacturers and Traders.

Note:
1. The 2022 and 2021 combined operating ratio used is for ongoing operations (see footnote 1 on page 25).