

Sustainability and the Three Lines – A Practical Perspective

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Sustainability regulation has become one of the most dynamic areas of financial services regulation and supervision in Ireland. The Central Bank of Ireland (CBI) has made clear-through speeches, Dear CEO letters, thematic reviews, and its *Guidance on Climate Change Risks*, that sustainability is now a core prudential and conduct priority. For compliance professionals, the challenge is no longer simply interpreting EU sustainable finance rules; it is ensuring that sustainability risks and obligations are embedded into the organisation’s governance, culture, and risk management architecture. The Three Lines model remains the backbone of this architecture, but sustainability risk and compliance management requires a more integrated, forwardlooking approach than many firms have historically applied.

Sustainability has been defined as *‘meeting the needs of the present without compromising the ability of future generations to meet their own needs’*, (Brundtland, 1987). Most readers will be familiar with the ‘Three Lines of Defence’ model where the First Line (business and operations) owns and manages risks and controls; the Second Line (risk and compliance functions) sets frameworks, oversees and challenges; and the Third Line (internal audit) provides independent assurance to the Board on how well risk and control frameworks actually work. This has evolved into the ‘Three Lines’ model but does not alter the fundamental allocation between; ownership, oversight, and assurance.

This article explores how Irish firms can embed sustainability into the Three Lines in a way that aligns with CBI expectations and strengthens risk management and overall governance.

1. First Line: Ownership, Implementation, and Cultural Change

The CBI has emphasised that climate remains a supervisory priority (Central Bank of Ireland, 2025) and climate and environmental risks must be treated like any other material risk, owned and managed by the business and effectively managed and mitigated, with Board ownership and a climate risk aware culture.

Key responsibilities for the First Line

- **Integrate sustainability into product governance and distribution**
The CBI expects firms to ensure that sustainability characteristics are accurately reflected in product design, target market assessments, and ongoing monitoring. Misalignment between product claims and underlying data is a key greenwashing risk.
- **Embed sustainability preferences into suitability assessments**
As customer awareness of and demand for sustainable products increases, the CBI has amended the Minimum Competency Code (effective January 2025) to include sustainability, which is now included as a staff competence. Under MiFID II and the revised Consumer Protection Code 2025 (effective 24 March 2026), customer sustainability preferences must be recorded in suitability assessments.
- **Strengthen sustainability data capture and operational controls**
The First Line must ensure data completeness, accuracy, and traceability, particularly when relying on external sustainability data providers.



- **Implement CBI expectations on climate risk integration**
The CBI's guidance requires firms to integrate climate risk into strategy, governance, risk management, and scenario analysis. This includes identifying material risks, assessing and managing, and embedding mitigants into daytoday decisionmaking and processes and procedures.

The First Line should move from considering sustainability as a compliance requirement to it being a core business risk and a key conduct or ethical responsibility reflecting the CBI's emphasis on accountability and senior management responsibility in a post Individual Accountability Framework world.

2. Second Line: Oversight, Challenge, and Regulatory Interpretation

The Second Line, risk, compliance, and sustainability oversight—plays a pivotal role in ensuring that sustainability risks are managed in line with CBI and wider stakeholder expectations.

Key responsibilities for the Second Line

- **Develop sustainability risk frameworks aligned with CBI expectations**
The CBI expects firms to understand its climate and sustainability risk profile and to embed those risks in its risk management framework.
- **Maintain robust regulatory horizon scanning**
As compliance professionals have observed since the EU Green Deal and with adjustments throughout 2025, the EU sustainable finance framework continues to evolve at pace. The extent and rate of regulatory change in sustainability means that the role of upstream management is especially critical in the sustainability domain, and a robust process will be critical to managing the associated regulatory risks.
- **Challenge sustainability disclosures and prevent greenwashing**
The CBI has signalled that greenwashing is a

supervisory priority. The Second Line must scrutinise the Sustainable Finance Disclosure Regulation (SFDR)¹, marketing materials, and product labels to ensure accuracy and consistency and conformance with regulatory frameworks.

- **Integrate sustainability into enterprise risk management**
The CBI expects firms to embed climate and environmental risks into risk appetite, stress testing, scenario analysis, and Board reporting (Central Bank of Ireland, 2021). The Second Line role is to ensure these expectations are met consistently.

The Second Line must serve not just as a compliance rule interpreter to a strategic advisor, helping the organisation navigate sustainability regulatory developments, risk profile evolution, evolving stakeholder expectations and increasing complexity.

3. Third Line: Independent Assurance and Supervisory Alignment

Internal audit plays a critical role in providing independent assurance that sustainability frameworks and controls are effective and aligned with CBI expectations.

Key responsibilities for the Third Line

- **Audit sustainability governance and Board oversight**
The CBI expects Boards to demonstrate active engagement with sustainability risks. Internal audit should assess whether governance structures support informed and timely sustainability decisionmaking.
- **Provide assurance over sustainability reporting**
As the Corporate Sustainability Reporting Directive (CSRD) reporting rolls out, albeit with a reduction in the number of firms in scope, internal audit must evaluate data integrity, reporting processes, and control effectiveness.
- **Assess integration of sustainability into risk management**
Internal audit should test whether sustainability risks are embedded into risk assessments, control frameworks, and monitoring.
- **Evaluate greenwashing controls**
Independent testing of product claims, disclosures, and marketing materials is essential to mitigate regulatory and reputational risk.

4. Considerations across all Three Lines:

- **Strategy:** Has sustainability been captured in the business strategy and supporting operations and business processes?
- **Culture:** Are sustainability objectives captured in a firm's employee processes (e.g. values, expected behaviours, goals)
- **Skillsets:** Is there sufficient sustainability expertise across all Three Lines? E.g. Have the First Line sufficient knowledge and skill / training to understand and recognise sustainability risks?
- **Risk Management:** Are all sustainability risks captured in the firm's risk universe?
- **Reporting:** Are sustainability reporting processes effective?

Summary: Sustainability as a Driver of Stronger Governance and Risk Culture

Embedding sustainability into the Three Lines is not merely a regulatory requirement, it is an opportunity to strengthen governance, enhance transparency, and build longterm resilience.

For Irish financial services firms, the CBI's expectations create a clear mandate: sustainability must be integrated into the organisation's risk management architecture, not treated as a parallel discipline.

Compliance professionals have a leadership role to play; championing sustainability integration across all lines, challenging, and ensuring robust governance, they can help their firms navigate a future where sustainability is inseparable from sound risk management.

References

- Brundtland. (1987). *Our Common Future*. World Commission on Environment and Development.
- Central Bank of Ireland. (2021). *Dear CEO Letter Supervisory Expectations of Regulated Firms Regarding Climate and Other ESG Issues*. Dublin: Central Bank of Ireland.
- Central Bank of Ireland. (2025). *Regulatory and Supervisory Outlook 2025*. Dublin: Central Bank of Ireland.

REFERENCE

1. Noting that on 20th November 2025 the European Commission proposed a set of amendments to SFDR.