

# Bank of England

Dame Meg Hillier  
Chair, Treasury Committee  
House of Commons  
London  
SW1A 0AA

**Sarah Breeden**  
Deputy Governor, Financial Stability

1 April 2026

Dear Chair,

## Response to TSC inquiry report on AI in financial services

The Bank welcomes the Committee's inquiry into Artificial Intelligence in financial services.

We share the TSC's view that AI has broad, complex, and likely long-term implications for how the UK financial system serves the real economy. However, we do not agree with the TSC's characterisation that the Bank is taking a 'wait and see' approach to the use of AI in financial services. The Bank (including the PRA) is proactively promoting the responsible adoption of new technologies in the financial sector. In relation to AI specifically, and in light of the pace at which the technology is evolving, the PRA has taken steps to ensure existing regulation is flexible, outcomes-focussed and effective, and this approach has been specifically welcomed by the industry.<sup>1</sup> In addition, the Bank is evaluating and monitoring the potential financial stability implications of the investment in, and development and adoption of, AI. It is crucial that our regulatory approach remains risk-based, proportionate and effective. We will continue to monitor AI adoption closely and will not hesitate to act when justified.

---

<sup>1</sup> [Summary of AI roundtables - February 2026 | Bank of England](#)



The rest of this letter sets out (1) our approach to the use of AI in financial services; (2) our approach to risks from broader AI investment and adoption across the wider economy; and (3) our response to the TSC's recommendations for the Bank.

## 1. Our approach to the use of AI in financial services

Given the Bank's statutory objectives, we want to create an environment in which responsible adoption of AI can thrive and contribute to financial sector innovation, competition, competitiveness, and growth, whilst safeguarding the integrity of the financial system. We are taking a proactive and proportionate approach to achieving that goal. Given the rapid pace of AI development and adoption, we keep our approach under continuous review.

**Our microprudential work in pursuit of that goal dates back several years.** In 2022, we published a joint [Discussion Paper 5/22](#) with the FCA, setting out how our rules applied to the use of AI, and seeking views on how our regulatory framework might need to evolve. The [feedback we received](#) indicated that many respondents thought there were no regulatory barriers to the safe and responsible adoption of AI in the UK. Several other themes came through, including: that given the rapidly changing capabilities, live guidance or best practice could be helpful; the importance of coordination amongst regulators domestically and internationally; concerns on the increasing use of third-party models and data; and the need for ongoing industry engagement. This feedback continues to inform our ongoing approach. In 2023, we issued new [Model Risk Management Principles for banks](#), which are technology-agnostic and outcomes-focussed but deliberately included factors relevant to the use of AI models. We intend to build on this further in 2026, including by leveraging the insights on good practice we have gained through both our supervisory dialogue and broader engagement with firms (more detail below). In addition, the PRA has highlighted AI adoption in its [2026 supervisory priorities](#), meaning AI will be a key topic of exploration and scrutiny in our supervisory dialogues with firms.

**The Bank has also been pursuing a macroprudential programme of work on the impact of AI at the level of the financial system.** In April 2025, the Financial Policy Committee set out the ways by which [AI adoption in the financial sector could pose financial stability risks](#). The four AI-related areas of focus for the FPC are: (1) greater use of AI in banks' and insurers' core financial decision-making; (2) greater use of AI in financial markets; (3) operational risks in relation to AI service providers; and (4) the changing external cyber threat environment. Monitoring these areas of focus will allow the FPC to understand if any systemic risks are developing and to ensure that any interventions are calibrated appropriately to support the responsible adoption of AI. We have continued to build on this approach and the [FPC's April 2026 Record, published today](#), includes the Committee's latest assessment. Evidence suggests that financial system participants have not yet adopted more advanced forms of AI, such as

generative or agentic AI, in a manner that would present systemic risk. However, risks are likely to increase, potentially rapidly, amid growing intent among financial firms to grow their deployment of advanced AI. The FPC supports the Bank's and the FCA's initiatives to continue monitoring the adoption of AI by regulated firms and has asked them to undertake further work on agentic AI, focused on use cases in payments and financial markets.

**All of this has been underpinned by our active monitoring through ongoing engagement with practitioners and experts.** This ongoing engagement is crucial to ensure we understand both the state of current adoption and the trajectory of future adoption, such that we are equipped to manage risks that may emerge in future. This year we will run the fourth edition of the [Bank and FCA's biennial survey of AI adoption by the financial sector](#); this survey provides crucial ongoing insight and analysis into AI use by Bank and FCA-regulated firms. In May last year, we and the FCA established the [AI Consortium](#), a platform for public-private engagement to gather input from stakeholders on the capabilities, development, deployment and use of AI in UK financial services. Through the Consortium, members are pursuing work to explore and identify approaches to support better management of key risks to the financial system arising from its use of AI, with [specific work on](#) (i) concentration risks including from third-party model providers, (ii) the evolution of AI 'edge cases', as adoption moves into use cases more relevant for financial stability such as credit risk assessment and trading, (iii) explainability and transparency in generative AI, and (iv) AI accelerated contagion in financial markets, as well as discussions on emerging trends such as the rise of agentic AI. The Consortium will publish a report on its work, including these areas of focus, this year.

In addition, through our co-chairing of the [Cross Market Operational Resilience Group](#), made up of authorities and industry, we continue to support its AI Taskforce, created in 2024. In May last year, the AI Taskforce published an [AI Baseline Guidance Review](#), which brought together existing guidance and good practice on how financial firms should mitigate operational and other risks from their adoption of AI. The Taskforce has since published a [Shared Responsibility Model](#), which provides an agreed baseline structure for managing security risks between AI service providers and financial services firms. It has also [published two severe-but-plausible cyber risk scenarios](#), based on the use by attackers of new AI technologies, to support firm testing and preparedness.

The above has been supplemented with additional structured engagement with a wide range of firms. Late last year, we conducted three [roundtables](#) with participants from regulated firms to better understand the constraints firms may be facing in adopting AI, and how the Bank and PRA can support responsible AI adoption. Each roundtable was held with representatives from a different PRA-regulated sector: (1) challenger banks

and UK-focussed larger banks; (2) global systemically important banks; and (3) insurers. These provided important insights for our future work, including on industry support for the PRA's regulatory framework as it relates to AI and on the need for risk management practice to evolve as more complex AI is deployed. We intend to repeat the exercise this year. Separately, the PRA held **two roundtable sessions in October with Chief Risk Officers** from some of the largest PRA-regulated firms to discuss the adoption of artificial intelligence and machine learning technologies in the context of implementing the principles set out in SS1/23 'Model risk management principles for banks' as supervisory expectation. The PRA presented thoughts on specific topics for AI and machine learning (ML), including risk appetite, model tiering, explainability and interpretability, data and overfitting, independent validation, and ongoing model monitoring. In addition, we conduct ad hoc rounds of meetings with market participants to understand the latest uses of AI in financial markets, particularly to seek the perspective of firms beyond our regulatory perimeter, via the Bank's **Market Intelligence** activities, which also informs our financial stability work.

**We are also actively collaborating with domestic and international authorities on the use of AI in the financial system.** This year, the G20 Financial Stability Board, chaired by the Bank's Governor Andrew Bailey, is prioritising work with international standard-setters on **sound practices for AI adoption, use, and innovation by financial institutions**.<sup>2</sup> The PRA acts as a co-chair of the International Association of Insurance Supervisors' (IAIS) AI workstreams, helping provide guidance and standards to support national regulators and supervisors in managing AI-related risks effectively. The Bank is working with the G7, via its cyber expert group, to manage the **risks that AI could pose to cybersecurity**. Domestically, we continue to work closely with the **AI Security Institute** to better understand potential financial stability risks involving frontier AI agents, as well as with the **Digital Regulation Cooperation Forum (DRCF)**.

**The Bank also uses AI, where appropriate, to support and enhance our own capabilities.** For example, the Bank uses AI for predictive analytics, the study of non-linear interactions between variables, and analysis of larger and richer data sets, which can potentially help forecast – for example - GDP growth and bank distress. We have also rolled out off-the-shelf AI assistants across the Bank, delivering productivity gains in a range of tasks including summarisation, note-taking, and code generation. Where needed, we are also building bespoke AI solutions. For instance, the PRA is actively

---

<sup>2</sup> We previously contributed to the FSB's reports on: **Artificial intelligence and machine learning in financial services** in 2017, **The Financial Stability Implications of Artificial Intelligence** in in November 2024, **Monitoring Adoption of Artificial Intelligence and Related Vulnerabilities in the Financial Sector** in October 2025.

exploring the use of LLMs to enhance supervisory tools, supporting tasks such as data extraction and natural language querying.

Through this considerable programme of work to date, we are keeping under review our technology-agnostic approach to regulation and whether further action or guardrails might be needed to promote the responsible adoption of AI in the financial sector - including in light of how rapidly the technology, its use cases and adoption levels are advancing.

## **2. Our approach to potential financial stability risks from broader AI investment and adoption across the wider economy**

Beyond the use of AI in financial services, given its statutory objectives, the Bank is also focussed on the potential opportunities and risks posed by the investment in, and adoption of, AI across financial markets and the wider economy.

In the [FPC's October 2025 Record](#), and then in its [Dec 2025 Financial Stability Report](#), we first flagged, and then published analysis of, the potential financial stability risks posed by a sharp decline in AI-related asset prices. The FPC noted that, while AI infrastructure investment has mostly been financed by the cash flows of large, profitable technology companies and equity investments to date, debt financing is increasing quickly, in ways that include a material contribution from private markets. If debt financing of AI development increases as projected this decade, the financial stability consequences to the UK economy of any AI-driven fall in asset prices could increase.

In addition, as noted in the [FPC's April 2026 Record](#), price moves in financial markets have highlighted that there are also risks to valuations for companies whose business models could be disrupted by AI. Such concerns, in the context of news around rapid AI innovation, contributed to sell-offs in software stocks earlier in the year. Concerns about potential disruption from AI also have implications in risky credit markets, particularly in private credit where growing exposures to the software sector have contributed to recent concerns over asset quality and valuation uncertainty.

The FPC will continue to monitor these risks closely.

## **3. TSC recommendations for the Bank**

***Recommendation:** To build firms' readiness for AI-driven market shocks, the Bank of England and the Financial Conduct Authority must conduct AI-specific stress testing.*

As noted in [the FPC's April 2025 Financial Stability In Focus](#) publication, we agree that stress testing and scenario analysis are valuable tools for understanding the risks

and opportunities offered by AI – particularly given the uncertainty in the future path of AI capabilities and adoption.<sup>3</sup>

The Bank is undertaking scenario analysis to guide its thinking and evaluation of the potential range and distribution of plausible macroeconomic and core financial market outcomes arising from AI investment, development, and adoption, and accompanying risks to UK financial stability. This scenario analysis will help ensure that a wide range of plausible outcomes arising from AI investment, development, and adoption scenarios are encompassed by the Bank's broader approach to stress testing, including system-wide exercises. In addition, we are working to incorporate AI scenarios into various forms of cyber and operational testing of the financial sector.

Separately, the Bank is pursuing work on simulation methods with international counterparts to better understand the conditions under which AI agents trading in financial markets could demonstrate correlated behaviour or 'herding' and so potentially exacerbate procyclical dynamics to amplify a stress scenario. This work could also explore how such dynamics could be mitigated, for example through exploring how agents' objective functions should best take account of public policy objectives.

***Recommendation:** By the end of 2026, HM Treasury must designate the major AI and cloud providers as critical third parties for the purposes of the Critical Third Parties Regime. Over a year since the regime was established, it is not clear to us why HM Treasury has been so slow to use the new powers at its disposal. The Bank of England's Financial Policy Committee must monitor the regime's progress and, if necessary, use its power of recommendation to HM Treasury to ensure swift implementation.*

In November 2024, the Bank, PRA and FCA published [SS6/24 Critical third parties to the UK financial system](#) which provided [final policy and rules for Critical Third Parties](#) (CTPs), as well as information on how they will approach CTP oversight. The overall objective of the oversight regime for CTPs is to manage risks to the stability of, or confidence in, the UK financial system that may arise due to a failure in, or disruption to, the services that a CTP provides to regulated firms and FMIs. If a third-party provider of AI services is deemed to pose financial stability risks were those AI services to fail or experience disruption, that third-party provider could be designated as a CTP.

As the Bank noted in the [December 2025 FSR](#), while no designations have been made to date, preparations are advancing and HM Treasury officials are in the process of gathering the necessary evidence to support decision making on designation. The

---

<sup>3</sup> The potential value of AI-related stress testing is also discussed in [Sarah Breeden's Engaging with the Machine: AI and Financial Stability October 2024 speech](#) and [external FPC member Jonathan Hall's oral evidence to the TSC's inquiry](#).

authorities remain committed to delivering the CTP regime successfully and the FPC will continue to monitor its implementation and outcomes with a focus on the impact of the regime on reducing the systemic risks posed by CTPs.

## Conclusion

Far from taking a 'wait and see' approach, we have invested heavily in analysing the current and future risks posed by both (i) the use of AI in financial services and (ii) the broader investment in and adoption of AI across the wider economy. We will continue to monitor closely adoption of AI in the financial sector and any risks this could pose, and keep under active review where we may need to adapt our regulatory and macroprudential approach, continuing to take a risk-based, proactive and proportionate approach as we do so.

We welcome and support the Committee's focus on this important matter.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Sarah Breeden', with a stylized, cursive script.

Sarah Breeden  
Deputy Governor, Financial Stability