



June 3, 2022

VIA ELECTRONIC SUBMISSION

James P. Sheesley
Assistant Executive Secretary
Attention: Comments—RIN 3064—ZA32
Federal Deposit Insurance Corporation
550 17th Street NW
Washington, DC 20429

Re: Principles for Climate-Related Financial Risk Management for Large Financial Institutions (RIN 3064—ZA32)

Ladies and Gentlemen:

The Financial Services Forum (the “Forum”)¹ appreciates the opportunity to submit this letter to the Federal Deposit Insurance Corporation (the “FDIC”) on its proposed principles (the “Proposal”) for climate-related financial risk management for large financial institutions. The Proposal is relevant to each of our member institutions, the eight U.S. global systemically important bank holding companies (“U.S. GSIBs”).

At the outset, we wish to highlight that we welcome the Proposal, subject to certain changes discussed further below, for a number of reasons. Our members recognize the need for banks to have robust capabilities for the safe and sound management of exposures to climate-related financial risks, and in fact, already have taken important steps to incorporate such risks into their comprehensive, enterprise risk management frameworks. Accordingly, the Forum supports the FDIC’s efforts, as well as the efforts of the Office of the Comptroller of the Currency (the “OCC”), to establish guidance for banks to address climate-related financial risks.

¹ The Financial Services Forum is an economic policy and advocacy organization whose members are the chief executive officers of the eight largest and most diversified financial institutions headquartered in the United States. Forum member institutions are a leading source of lending and investment in the United States and serve millions of consumers, businesses, investors, and communities throughout the country. The Forum promotes policies that support savings and investment, deep and liquid capital markets, a competitive global marketplace and a sound financial system.

Below, we comment on the specific principles from the Proposal that we support and highlight areas where the FDIC's guidance in the Proposal could be recalibrated. We also provide responses to certain questions posed by the FDIC throughout our letter, as indicated. Our key observations and recommendations are as follows:

- **We welcome the guidance.** The Forum recognizes the emerging risks to banks presented by climate change and the importance of having robust capabilities to manage banks' exposures to such risks. Indeed, our member institutions already have taken steps to incorporate climate-related financial risks into their risk management frameworks. The Proposal is helpful for understanding the FDIC's particular areas of focus with respect to the management of climate-related financial risks, and we welcome FDIC guidance in this area as our member institutions work on strengthening and refining their climate-related financial risk management processes over time.
- **Support for scenario analysis rather than traditional stress testing.** The Forum supports the use of scenario analysis, which can provide insights into a range of tailored scenarios. Scenario analysis should focus on material exposures and incorporate plausible scenarios, particularly with respect to transition risk. We also appreciate the distinction the Proposal makes between scenario analysis and traditional stress testing, which could result in adverse regulatory consequences, as gaps in data availability and methodology make regulatory consequences inappropriate.
- **Support for principles and risk-based, flexible approach.** The Forum supports high-level principles that enable banks to have flexibility to incorporate climate-related financial risks into their existing risk management frameworks and processes where appropriate. In addition, we support a risk-based approach that considers the unique characteristics of each bank and allows banks to focus on targeting material climate-related financial risks. Given the evolving nature of the risks, data and tools, we also urge the FDIC to adopt a "phased approach" so that banks have sufficient time to meet supervisory expectations, in particular relating to incorporation of and reliance on quantitative metrics.
- **Oppose a new requirement to consider impacts on broader aspects of the economy.** The Proposal seemingly introduces a novel requirement in the introductory preamble language, stating: "the manner in which financial institutions manage climate-related financial risks to address safety and soundness concerns should also seek to reduce or mitigate the impact that management of these risks may have on broader aspects of the economy."² This requirement

² Statement of Principles for Climate-Related Financial Risk Management for Large Financial Institutions, 87 Fed. Reg. 19507, 19509 (Apr. 4, 2022).

appears to be sweepingly broad and vague, and without statutory basis.³ Moreover, it would be inappropriate for the FDIC to expect financial institutions as part of their risk management practices to consider impacts on the broader economy, which could conflict with the institution's practices that are necessary to promote safety and soundness. Accordingly, we recommend that the final guidance eliminate this language from the preamble.

1. We support the Proposal's endorsement of scenario analysis, in particular, rather than regulatory stress testing, to assess and manage climate-related financial risks.

- a. Scenario analysis is the preferred method of evaluating climate-related financial risks.

The Proposal recommends scenario analysis as an “important approach for identifying, measuring, and managing climate-related risks.” In doing so, the Proposal explicitly distinguishes scenario analysis from “traditional stress testing exercises that typically assess the potential impacts of transitory shocks to near-term economic and financial conditions.” We agree that scenario analysis is more appropriate than traditional stress testing, and this approach is consistent with the approaches supported by other U.S. regulators, including OCC, Federal Reserve Board (“Federal Reserve”) and the Financial Stability Oversight Committee (“FSOC”).

Scenario analysis is a much more suitable tool to evaluate the potential economic and financial risks posed by different climate outcomes. A key difference between stress testing and scenario analysis is that traditional stress testing may be associated with regulatory requirements,⁴ with respect to which the failure to comply can result in supervisory consequences and limitations on capital distributions and discretionary bonus payments.⁵ As discussed in greater detail below, banks face significant challenges in identifying and measuring climate-related financial risks, particularly around data. Given the gaps in currently available data, models and methods used to assess climate-related financial risks, it would be inappropriate for banks to experience adverse regulatory consequences as a result of quantitative assessments that rely on currently available data and methodologies.

³ See, e.g., 12 U.S.C. § 1831p-1.

⁴ See, e.g., Financial Stability Oversight Council, Report on Climate-Related Financial Risk, at 90 (Oct. 2021) [hereinafter, “FSOC Report”]; Jerome Powell Remarks, Green Swan Conference, hosted by the Bank for International Settlements (Jun. 4, 2021) [hereinafter, “Powell Remarks”] (stating that scenario analysis is “not meant to be setting up a regulatory consequence, which obviously does flow from our regulatory stress tests”).

⁵ 12 C.F.R. 217.11(c)(1).

In contrast, scenario analysis does not necessarily result in direct regulatory consequences and “may contemplate much longer time horizons in order to assess medium- and long-term business model resilience against the changes in climate-related risks that may materialize over such longer horizons.”⁶ Stress testing necessarily tends to focus on shorter time horizons⁷ and would be unable to account for the fact that climate-related financial risks could “evolve over various time horizons,” including “those that extend beyond the bank’s typical strategic planning horizon,” as noted in the Proposal’s “Governance” principle. Therefore, a tool like scenario analysis, which can explore a range of potential scenarios over long-term horizons, would be better suited as a more flexible risk management tool for guarding against climate-related financial risks.

Lastly, the Federal Reserve has itself distinguished between scenario analysis and stress testing⁸ and is currently developing a program of climate-related scenario analysis.⁹ Federal Reserve Chair Jerome Powell in his re-nomination hearing reiterated support for scenario analysis rather than traditional stress tests: “I think it’s very likely that climate stress scenarios, as we like to call them, will be a key tool going forward. I would stress that those are very different from the regular stress tests which affect capital.”¹⁰ Governor Lael Brainard reiterated that she is not currently advocating including climate-related financial risks in traditional stress tests during her nomination hearing: “I certainly have not stated that we should do climate stress tests.”¹¹ The FSOC Report on Climate-Related Financial Risk (the “FSOC Report”) also strongly recommended that member agencies use scenario analysis, but stopped short of recommending climate stress testing akin to the Dodd-Frank Act Stress Tests or the Federal Reserve’s Comprehensive Capital Analysis and Review (“CCAR”) program.¹²

⁶ FSOC Report, *supra* note 4; *see also* Lael Brainard, “Financial Stability Implications of Climate Change” (Mar. 23, 2021), <https://www.federalreserve.gov/newsevents/speech/brainard20210323a.htm> [hereinafter, “Brainard Remarks”].

⁷ *See, e.g.*, FSOC Report, *supra* note 4 (noting that “stress tests within the remit of regulators tend to focus on a shorter time horizon in order to determine the solvency and liquidity of an institution given an ‘extreme but plausible’ market risk or set of macroeconomic shocks”); 12 C.F.R. 225.8(d)(16) (defining “planning horizon” for capital planning purposes to include a period of at least nine consecutive quarters); 12 C.F.R. 252.35(a)(4) (requiring liquidity stress testing to be conducted using overnight, 30-day, 90-day and one-year planning horizons).

⁸ *See, e.g.*, Powell Remarks, *supra* note 4; Brainard Remarks, *supra* note 6.

⁹ *See, e.g.*, Federal Reserve, Financial Stability Report, at 63 (Nov. 2021), <https://www.federalreserve.gov/publications/files/financial-stability-report-20211108.pdf>.

¹⁰ Senate Banking, Housing, and Urban Affairs Committee Nomination Hearing (Jan. 11, 2022).

¹¹ Senate Banking, Housing, and Urban Affairs Committee Nomination Hearing (Jan. 13, 2022).

¹² FSOC Report, *supra* note 4, at 90 (“Scenario analysis is similar to, but distinct from, stress testing as deployed by financial regulators, such as the supervisory Dodd-Frank Act Stress Tests of the Federal Reserve Board, OCC, and FDIC and the Comprehensive Capital Analysis and Review (CCAR) performed by the Federal Reserve Board on the largest banking organizations.”).

b. Response to questions regarding scenario analysis.¹³

The FDIC has asked for feedback on how banks currently use climate scenario analysis and which factors would be most salient to consider when designing these exercises in the future. We highlight some observations and challenges about climate scenario analysis based on the experience of our member institutions and recommend certain features of scenario analysis that the FDIC should support in its final guidance.

i. *Observations and challenges.*

- **Forum member institution practices.** Forum member institutions already engage in climate scenario analysis as part of their broader risk management program to measure, monitor and assess their exposure to climate-related financial risks. These analyses are focused on identifying and sizing climate-related financial risks in their asset portfolios so that these risks can be monitored and managed on an ongoing basis. In formulating climate scenarios, our member institutions focus their scenarios on the most prominent likely exposures that would be impacted by climate change, subjecting certain asset portfolios to climate scenario analysis rather than conducting enterprise-wide scenario analysis.

For example, some of our member institutions designed scenarios to examine the impacts of two short-term transition risk pathways on a sample portfolio of companies in the oil and gas value chain. One of these pathways was based on rapid electric vehicle adoption and the other was based on the adoption of a global carbon tax. Focusing on this portfolio allowed our member institutions to analyze the financial impacts of each pathway across different segments of the value chain within the oil and gas industry.

- **Gaps in data and modeling.** As discussed in greater detail below, existing data and tools to measure and quantify climate-related financial risk—and in particular longer-term transition and physical risks—are only just emerging, and will need to undergo substantial exploration, refinement and adaptation over time. Data gaps, and uncertainty given the unprecedented nature of climate change, present a significant challenge for banks because the reliability of the scenario analysis results depends on the reliability of the underlying data. While climate-related data has improved in both quantity and quality over the past several years, there are still considerable gaps that frustrate attempts to accurately identify climate-

¹³ This section is responsive to Questions 13 and 14 posed by the FDIC, respectively: “Scenario analysis is an important component of climate risk management that requires assumptions about plausible future states of the world. How do financial institutions use climate scenario models, analysis, or tools and what challenges do they face?” and “What factors are most salient for the FDIC to consider when designing and executing scenario analysis exercises?”

related financial risks. In particular, our member institutions have highlighted data gaps regarding physical risks, such as the possibility that specific locations will experience extreme weather events and the geographic location of physical assets of companies. One of our member institutions conducted a scenario analysis to identify areas exposed to significant physical risks by mapping the bank's exposures by geography and then cross-referencing these global geographies against potential hot spots for physical climate impacts. The more reliable the geographic data, the more useful such exercises will be.

As another example, publicly available climate scenarios do not provide banks with the appropriate sectoral and regional granularity to directly translate scenario output into readily consumable inputs for internal risk modeling. For banks, the value of climate scenario analysis can only be fully realized when the science-based or macroeconomic output is expanded into more granular financial impacts that can be applied across a diverse set of client industries and sub-sectors. There is also a limited understanding of the Integrated Assessment Models that drive these scenarios, which makes it more challenging for banks and vendors alike to expand scenario output while staying within the bounds of the model.

- **Time horizons.** The long-term nature of climate change poses significant challenges for modeling climate-related financial risks, but striking the right balance between accounting for long-term climate change and doing so within an actionable framework is critical. As discussed above, financial risks are generally considered over the short to medium-term horizon and are generally assessed over one to three years. Climate scenario analysis over substantially longer horizons presents two important challenges. First, risk management decisions are not generally made with respect to lengthy time horizons. Second, the uncertainty around risks of any type grow quickly with the time horizon. Long time horizons lead to a wide range of uncertainty about the evolution of climate-related financial risks that make interpreting any findings difficult. Relatedly, it is necessary to make assumptions about how the evolution of the climate will impact economic variables, such as trade, employment and the relative performance of different economic sectors. Making such forecasts in the near-term is difficult, and understanding how the distant evolution of the climate relates to various economic indicators is all the more challenging.

ii. Recommendations.

We recommend the following for the FDIC's final guidance regarding scenario analysis:

- **Phased approach.** As noted above, there are still significant data and modeling gaps that affect the reliability of scenario analysis results. Accordingly, as discussed further below, we support a phased approach to climate risk

management, including for climate scenario analysis, while data becomes more reliable, available and consistent.

- **Materiality thresholds should be incorporated.** A risk-based approach that considers the unique characteristics of each bank and that allows banks to focus on targeting material climate-related financial risks should apply to scenario analysis as well. The FDIC, for example, should permit banks to continue focusing their scenarios on the most material likely exposures that would be impacted by climate change, and subjecting only certain asset portfolios to climate scenario analysis.
- **Banks should have flexibility in designing scenarios.** Although we would appreciate high-level guidance on scenario analysis from regulators, we also recommend that the FDIC give banks flexibility in the design of their scenarios. This approach will ensure that the broad frame of the scenario is articulated comprehensively while allowing individual firms to tailor the scenarios to the specific needs of their asset portfolios.
- **Scenarios encompassing transition risks should be plausible.** Scenarios used for scenario analysis may be severe and rigorous but should also be credible. Scenarios keyed to tail risks that are too remote may result in risk measurements that are not highly relevant. Overall, the degree of severity in any climate scenario must be appropriately balanced against its plausibility. This balance should be made explicit in a well-articulated and measurable standard that should be employed to help ensure that climate scenarios, and in particular transition risks, are empirically relevant and have the potential to result in actionable outcomes. Transition risk may be even harder to predict than physical risk because it depends on the path of government policy. Moreover, different assumptions about the specific type and trajectory of policy can lead to significantly different outcomes. As an example, a transition risk scenario that considers the rapid imposition of a large and widely applicable carbon tax would have a significantly different impact than a transition risk scenario that is focused more narrowly on policies targeting the fossil fuel industry. FDIC guidance should provide clear, high-level guidance on the nature and extent of transition risk scenarios to be considered, and these scenarios should be plausible.

2. We support the Proposal’s flexibility in permitting climate-related financial risks to be incorporated into existing risk management frameworks.

- a. Climate-related financial risk may be effectively addressed within existing risk management frameworks, which already sufficiently account for climate-related financial risks.¹⁴

Climate-related financial risk may be considered a transverse, cross-cutting risk in some instances or a standalone risk in others. As a result, in some circumstances it may be more appropriate for banks to embed climate-related financial risks into existing risk management frameworks and in others to create new, standalone frameworks. The Proposal appears to permit the approach of incorporating climate-related financial risks into existing frameworks and systems where appropriate, and we believe the final guidance should retain this flexible perspective.

In the Proposal, the FDIC explains that the draft principles are “consistent with the risk management framework described in existing FDIC rules and guidance” and are intended to “help bank management make progress toward ... *incorporating climate-related financial risks into financial institutions’ risk management frameworks*” (emphasis added). The “Governance” principle explicitly contemplates that “[r]esponsibility and accountability may be integrated within existing organizational structures.”

As the Proposal acknowledges, existing risk management and corporate governance standards applicable to large U.S. banking organizations are sufficiently broad and flexible to accommodate climate-related financial risks as an integrated component. For example, the OCC safety and soundness regulations require large banks to update their risk governance frameworks “at least annually, and as often as needed to address ... changes in the [] bank’s risk profile caused by emerging risks.”¹⁵

¹⁴ This section is, in part, responsive to Questions 5 and 8 posed by the FDIC, respectively: “What specific tools or strategies have financial institutions used to successfully incorporate climate-related financial risks into their risk management frameworks?” and “What, if any, specific products, practices, and strategies—for example, insurance or derivatives contracts or other capital market instruments—do financial institutions use to hedge, transfer, or mitigate climate-related financial risks?”

¹⁵ OCC Guidelines Establishing Heightened Standards for Certain Large Insured National Banks, Insured Federal Savings Associations, and Insured Federal Branches; Integration of Regulations, 79 Fed. Reg. 54517 (Sept. 11, 2014) [hereinafter, “OCC Heightened Standards”]; *see also* Enhanced Prudential Standards for Bank Holding Companies and Foreign Banking Organizations, 79 Fed. Reg. 17239 (Mar. 27, 2014) [hereinafter, “Enhanced Prudential Standards”] (requiring that the risk management frameworks of a large U.S. bank holding company “be commensurate with its structure, risk profile, complexity, activities, and size,” and requiring subject institutions to implement broad frameworks rather than targeted responses to enumerated risks and to adjust their frameworks as risks and activities vary).

OCC regulations and standards also address many of the specific risk management and internal control elements promoted in the Proposal, including without limitation for board and senior management oversight, risk appetite framework, risk data aggregation and reporting and internal controls.¹⁶ Large U.S. banks are already expected to consider their material risks in capital planning, strategy development, credit portfolio management and liquidity management, as well as the impact of material and emerging risks on other risk categories, including liquidity, credit, market, strategic, operational and model risk.¹⁷

U.S. GSIBs, therefore, already have in place robust risk management frameworks and practices that are designed to address material risks and are purposefully flexible to enable the incorporation of responses to new and emerging risks. In fact, as would be the case for any other material risk, our member institutions already have been incorporating climate-related financial risk analysis into their risk management practices.¹⁸

Our member institutions have worked to incorporate oversight of climate-related financial risk into their existing governance structures by, in some instances, establishing internal committees that consist of senior executives with specific purview over climate-related financial risk management. For example, one of our member institutions has established a climate risk team that is responsible for developing the bank's internal approach to managing climate-related financial risk, with the goal of integrating climate considerations into existing risk management frameworks.

Forum member institutions employ a variety of effective strategies to mitigate climate-related financial risks and already generally prioritize risk management of assets and

¹⁶ See, e.g., OCC Heightened Standards, *supra* note 15; OCC, Comptroller's Handbook: Corporate and Risk Governance (July 25, 2019), <https://www.occ.treas.gov/news-issuances/bulletins/2019/bulletin-2019-38.html> [hereinafter, "OCC Corporate and Risk Governance Handbook"]; Enhanced Prudential Standards, *supra* note 15; Federal Reserve, SR 21-3 / CA 21-1: Supervisory Guidance on Board of Directors' Effectiveness (Feb. 26, 2021) [hereinafter, "Federal Reserve SR 21-3"]; Federal Reserve Board, Bank Holding Company Supervision Manual (Nov. 2021) (risk management processes and internal controls), <https://www.federalreserve.gov/publications/files/bhc.pdf>.

¹⁷ See, e.g., OCC Heightened Standards, *supra* note 15; OCC Corporate and Risk Governance Handbook, *supra* note 16; Enhanced Prudential Standards (managing liquidity risk), *supra* note 15; Federal Reserve SR 21-3, *supra* note 14; 12 C.F.R. 225.8(e)(2)(ii)(A); Federal Reserve, SR 15-18: Federal Reserve Supervisory Assessment of Capital Planning and Positions for Firms Subject to Category I Standards (revised Jan. 15, 2021); Federal Reserve, SR 15-19: Federal Reserve Supervisory Assessment of Capital Planning and Positions for Firms Subject to Category II or III Standards (revised Jan. 15, 2021); Federal Reserve, SR 10-6: Interagency Policy Statement on Funding and Liquidity Risk Management (Mar. 17, 2010).

¹⁸ We also note that, to some extent, banks have historically been successfully managing climate-related risks in conducting their activities. See, e.g., Kristian S. Blickle et al., Federal Reserve Bank of New York, How Bad Are Weather Disasters for Banks?, at 3 (Nov. 2021) [hereinafter, "NY Fed Staff Report"] (discussing that "long run sea level rise may have already been priced into coastal properties" and that "counties more exposed to sea level risk pay higher underwriting fees for bonds").

clients in industries considered to be higher risk or high-carbon intensity. For example, to address idiosyncratic flood risk, our member institutions generally have policies in place to require flood insurance when underwriting a mortgage if the location of the property is in a flood plain. Some of our member institutions are also taking into consideration the client's intended use of financing, geographic locations of operations and ability to manage potential physical risk impacts. Further, some of our member institutions incorporate climate-related financial risks into overall credit assessment and underwriting processes for certain industries and loans, like commercial real estate and mortgages.

The Proposal suggests a new requirement for credit risk: "The board and management should determine credit risk appetite and lending limits related to these [climate-related financial] risks."¹⁹ In line with existing risk identification processes, banks are appropriately considering impacts of climate-related financial risks on the overall risk appetite of the firm. We do not think guidance should be so prescriptive as to require changes to existing, or creation of new, credit risk appetite and lending limits as a result of climate-related financial risk considerations. As mentioned above, Forum member institutions incorporate climate-related financial risks in their existing risk-management programs, including credit assessments, and the final guidance should not mandate that banks establish prescriptive lending limits.

In addition, we do not believe that a new type of regulatory or other external reporting specifically directed at climate-related financial risk by banks from the banking regulators is necessary at this point in time.²⁰ All of our member institutions are already engaged in voluntary reporting efforts through the Taskforce on Climate-Related Financial Disclosures ("TCFD") as well as other industry-led reporting frameworks.²¹ In addition, the Securities and Exchange Commission (the "SEC") has proposed disclosure rules for the enhancement and standardization of climate-related disclosures; the Forum will be submitting comments on that proposal.²²

In short, the final guidance should retain the Proposal's approach of allowing banks the flexibility to treat climate-related financial risk as a risk that may be integrated into

¹⁹ 87 Fed. Reg. at 19511.

²⁰ This is responsive to Question 12 posed by the FDIC: "How could existing regulatory reporting requirements be augmented to better capture financial institutions' exposure to climate-related financial risks?"

²¹ See TCFD, Core Recommendations, <https://www.fsb-tcfd.org/recommendations/#core-recommendations>; Carbon Disclosure Project, Climate Change 2021 Questionnaire (Jan. 2021), <https://guidance.cdp.net/en/guidance?cid=18&ctype=theme&idtype=ThemeID&incchild=1µsite=0&otype=Questionnaire&tags=TAG-13071%2CTAG-605%2CTAG-600>.

²² See SEC, The Enhancement and Standardization of Climate-Related Disclosures for Investors, 87 Fed. Reg. 21334 (Apr. 4, 2022).

banks' existing risk management frameworks and reporting. This not only would be consistent with regulatory expectations that banks' risk management frameworks encompass all material risks to the bank,²³ but also would enable banks to more expeditiously address emerging climate-related financial risks.

- b. Time horizons should be consistent with how banks currently assess and mitigate risk.²⁴

The specific time horizon considered relevant for climate-related financial risks depends on the specific use for which the analysis is employed. A bank's risk management and stress testing time horizons generally are relatively short-term (e.g., less than three years and often far shorter), in order to facilitate meaningful and realistic risk appetite and business strategy planning. The Basel Committee on Banking Supervision ("BCBS") explains that traditional financial risk scenario analysis and stress testing use shorter time frames because the uncertainty of the results increases with the timespan, as more assumptions are required.²⁵

As the Proposal's Governance principle states, climate-related financial risks could "evolve over various time horizons," including "those that extend beyond the institution's typical strategic planning horizon." Although we agree climate change is a long-term phenomenon, expectations around climate-related financial risk management should seek a balance between the uncertain long-term effects of climate change and the need for bank management to address the more immediate impacts in an effective manner consistent with risk appetite and business planning. For example, a 30-year time horizon would be inconsistent with the risk management frameworks used by our member institutions.

We recognize that scenario analyses may be conducted over longer time horizons, as discussed above, but the time horizons used in overall climate-related financial risk management frameworks should be consistent with current approaches to risk management in order to facilitate incorporating climate-related financial risks into existing practices. Accordingly, we recommend that the final guidance give banks flexibility to determine the appropriate time horizon depending on the purpose of the analysis.

²³ See, e.g., OCC Heightened Standards, *supra* note 15.

²⁴ This section is, in part, responsive to Question 7 posed by the FDIC: "What time horizons do banks consider relevant when identifying and assessing the materiality of climate-related financial risks?"

²⁵ See Basel Committee on Banking Supervision, Climate-Related Financial Risks – Measurement Methodologies (Apr. 2021), at 20–21, <https://www.bis.org/bcbs/publ/d518.pdf>; Federal Reserve, The Supervisory Capital Assessment Program: Design and Implementation (Apr. 24, 2009), at 3, <https://www.federalreserve.gov/newsevents/pressreleases/files/bcreg20090424a1.pdf>.

3. We support the principles and risk-based framework discussed in the Proposal and believe the final guidance should reflect this framework and allow banks to focus on climate-related financial risks that are material to them.

In the introduction to the Proposal, the FDIC explains that the draft principles are intended to provide a “*high-level framework* for the safe and sound management of exposures to climate-related financial risks” and to support banks’ efforts “to focus on key aspects of climate risk management” (emphasis added). The FDIC also notes that, “[i]n keeping with the FDIC’s risk-based approach to supervision, the FDIC intends to appropriately tailor any resulting supervisory expectations to reflect differences in banks’ circumstances such as complexity of operations and business models.” The “Scenario Analysis” principle also advises that management develop and implement scenario analysis frameworks “in a manner commensurate to the institution’s size, complexity, business activity, and risk profile.”

We support the use of these risk-based principles to support banks’ efforts to manage and mitigate climate-related financial risks. A risk-based framework will enable firms to tailor the incorporation of climate-related financial risks into their risk management frameworks based on a particular firm’s size, as well as the unique nature, scale and complexity of its activities and business.

For example, we recognize that size and complexity of banking organizations can be correlated with their potential to pose systemic risk. For this reason, U.S. GSIBs are taking climate-related financial risks very seriously and already have taken certain steps to account for such risks in their governance and risk management frameworks. That said, there may be instances in which larger banks are less vulnerable to losses resulting from climate disaster. Notably, a recent staff report released by Federal Reserve Bank of New York economists (“[NY Fed Staff Report](#)”) revealed that, in the case of extreme weather events over the last quarter century, “losses at larger (multi-county) banks [were] barely affected and their income increase[d] significantly with exposure,” whereas local banks, which do not benefit from diversification across multiple geographies, experienced more negative stability effects from extreme disasters.²⁶

The flexibility that would be provided by a principles and risk-based framework would allow each firm to focus on aspects of climate-related financial risks that are material to the particular firm and avoid diverting resources to aspects that present less risk based on the unique characteristics and activities of the firm. For example, certain financial instruments may not generate material climate-related financial risk, such as short-term liquid financial instruments for which pricing and value at risk metrics already capture the risk. While our member institutions will certainly be monitoring for all categories of

²⁶ NY Fed Staff Report, *supra* note 18, at 1.

risks and adjusting their internal controls as appropriate, focusing on the key material risks within key affected business lines will allow our member institutions to manage their exposure to climate-related financial risks in a manner that is most targeted and efficient.

It is important that Forum member institutions be allowed to leverage existing risk management practices and capabilities in assessing the materiality of an asset portfolio in relation to climate-related risk management. For example, our member institutions have identified a variety of material climate-related financial risks based on their distinct portfolios and exposures.²⁷ Our member institutions generally have developed a process to determine whether a risk is material that consists of: (1) identifying and assessing the potential impacts of a risk, (2) ranking the likelihood of the occurrence of the particular risk, (3) assessing and measuring the risk and (4) then making decisions based on that assessment. The material risks identified through this process inform the bank's scenario design and analysis, risk appetite and strategic planning.

Another example of a materiality determination is identifying portfolio sensitivity to climate-related financial risks through both qualitative and quantitative analyses to gauge the materiality of an asset portfolio's sensitivity to climate change, such as rising sea levels and increased incidences of extreme weather events, like wild fires and hurricanes. This process often makes use of highly granular data, including the precise location of an asset and its relation to relevant geographic features, such as proximity to a floodplain or wildfire prone areas. These analyses are then used to build an overall assessment of a portfolio's sensitivity to climate-related financial risks, which is then used to determine if more intensive and granular scenario analysis would be warranted from a risk measurement and management perspective.

4. The final guidance should adopt a phased approach to requiring banks to incorporate certain practices into their risk management frameworks.

For reasons discussed below, we believe the process for meeting supervisory expectations regarding climate-related financial risks should be an iterative process.

First, we note that this specific guidance on climate-related financial risks is new, although it draws from existing, more general guidelines. Accordingly, an appropriate timeframe will be required for banks to fully incorporate the practices discussed in the Proposal into their risk management frameworks and systems.

Second, banks face a number of challenges in addressing climate-related financial risks, including the following:

²⁷ This paragraph is, in part, responsive to Question 6 posed by the FDIC: "How do financial institutions determine when climate-related financial risks are material and warrant greater than routine attention by the board and management?"

- Limitations on data, in particular, data “connecting the science of climate change to financial risk assessments and real-world economic impacts”,²⁸
- The relatively new and evolving nature of models and methods employed for climate scenario analysis relative to those used in traditional financial stress testing, which may not currently be suitable for rigorously assessing granular climate-related financial risks;
- Uncertainty about the time horizons over which certain risks (*e.g.*, transition risks, longer-term risks) may manifest;²⁹ and
- The non-linear and complex nature of the impacts of climate change, which make it difficult to forecast the frequency and intensity of severe climate events and assess the interlinkages between climate-related pathways and economic and financial variables across the financial system.³⁰

The FSOC Report included a lengthy discussion of the challenges associated with identifying and mitigating climate-related financial risks, particularly around data. The FSOC Report stated that “enhancing the availability of and access to relevant, comprehensive data and developing methods and metrics to effectively utilize climate-related data and financial data” are “[n]ecessary steps for measuring and assessing climate-related financial risk.”³¹

These challenges, as well as the evolving nature of climate-related financial risks, necessitate an ongoing process for managing such risks. The Proposal in fact states that “[t]he FDIC recognizes that the incorporation of material climate-related financial risks into various planning processes is iterative as measurement methodologies, models, and data for analyzing these risks continue to evolve and mature over time.”³² Guidance should take into account the limitations around currently available data and metrics when setting expectations for banks.

To account for the time required for, and the challenges associated with, integrating climate-related financial risks into banks’ risk management practices, we recommend that the FDIC adopt an iterative or “phased approach.” This would involve the FDIC phasing in certain expectations as the data and tools become more reliable and in recognition that

²⁸ FSOC Report, *supra* note 4, at 23. These challenges are discussed in the FSOC Report as examples of challenges that *regulators* face, but we believe they are also applicable to banks.

²⁹ *Id.*

³⁰ *Id.*

³¹ *Id.* at 47.

³² Proposal, “Strategic Planning” principle.

banks will require transition periods to address emerging climate-related financial risks. In particular, we strongly recommend that the final guidance explicitly recognize that some expectations outlined in the principles cannot be executed based on quantitative rather than qualitative metrics until banks have sufficient time to develop capabilities and data and measurement tools have advanced to the degree that they can be sufficiently relied upon to serve as a basis for a number of the expectations specified in the guidelines. For example, it would not currently be appropriate to incorporate climate-related financial risks into capital and liquidity planning processes. It is important that there be sufficient flexibility in climate modeling standards so that learning and innovation can occur on an ongoing basis. A phased approach that clearly sets out gradual milestones for certain expectations would best reflect the evolving nature of climate-related financial risks and support banks' efforts to manage climate-related financial risks in a manner that is effective, accurate and methodical.

5. Certain of the principles and commentary should be clarified in the final guidance.

We recommend that certain of the principles and commentary be clarified further in the final guidance.

a. Governance.

For the "Governance" principle, the FDIC should distinguish the roles and responsibilities of bank boards and management with respect to risk management. We believe the FDIC should coordinate with the OCC and the Federal Reserve to ensure consistency with respect to the scope of a board's responsibility to oversee other risks facing a financial institution.³³

b. Public communication.

For the "Strategic Planning" principle, the FDIC should clarify the language regarding public communication of climate-related strategies. The Proposal calls for banks to "ensure that any public statements about an institution's climate-related strategies and commitments are consistent with their internal strategies and risk appetite statements."³⁴ Specifically, we believe it would be more appropriate for each bank to ensure that public communication of its climate-related strategies is consistent with *the actions the bank is actually taking*. This focus on accuracy aligns with the U.S. securities disclosure regime,

³³ See OCC, Director's Book: Role of Directors for National Banks and Federal Savings Associations (Nov. 2020), at 14–15, <https://www.occ.gov/publications-and-resources/publications/banker-education/files/directors-book.html>; Federal Reserve, SR 21-3 / CA 21-1: Supervisory Guidance on Board of Directors' Effectiveness (Feb. 26, 2021), <https://www.federalreserve.gov/supervisionreg/srletters/SR2103.htm>.

³⁴ Proposal, "Strategic Planning" principle.

which requires accuracy in public statements. We believe the current wording of this expectation would benefit from clarification by stating that the FDIC's focus in this area is having banks avoid making materially inaccurate or untrue public statements regarding climate-related financial risk plans, strategies or actions.

We also believe the responsibilities of the board and management with respect to public communications regarding climate-related strategies could benefit from clarification. The Proposal calls for both boards and management to "ensure" consistency between public communications and internal strategies regarding climate-related strategies. As boards do not review a bank's public communications except in extraordinary circumstances, we recommend that the final guidance not assign the board responsibility for ensuring alignment between public communications and internal climate-related strategies.

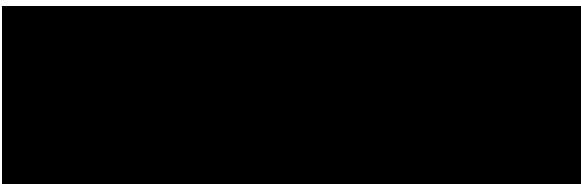
6. Regulatory agencies should cooperate so that there is one consistent set of high-level standards applicable across an entire banking organization.

Banking organizations benefit from a consistent set of guidelines from banking regulators. We also reiterate our support for guidance, like the Proposal, that is principles-based and high-level. We appreciate the FDIC's coordination with other financial regulators and in particular the similarities between the Proposal and the OCC's proposed principles on climate-related financial risk management.³⁵ We agree that the federal banking agencies should take a consistent and coordinated approach to high-level guidance relating to risk management frameworks for climate-related financial risk.

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Thank you for considering these comments. Please feel free to contact the undersigned (KFromer@fsforum.com) with any questions.

Respectfully submitted,



Kevin Fromer
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The Financial Services Forum

³⁵ OCC, Principles for Climate-Related Financial Risk Management for Large Banks (Dec. 16, 2021), <https://www.occ.gov/news-issuances/bulletins/2021/bulletin-2021-62a.pdf>.