U.S. Chamber of Commerce

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Basel Committee on Banking Supervision
Bank for International Settlements
CH-4002 Basel
Switzerland

Re: Principles for the effective management and supervision of climate-related financial risks

The U.S. Chamber of Commerce ("the Chamber") appreciates the opportunity to share our views in response to the Basel Committee on Banking Supervision ("BCBS" or "Committee") request for comment on its public consultation on principles for the effective management and supervision of climate-related financial risk ("principles").

The Chamber has been a leader in the conversation on environmental, social, and governance ("ESG") topics for nearly a decade, encouraging industries to work with investors on standards to meet investor interests and reflect the unique circumstances and contexts of industries and businesses. We continue to actively collaborate with our members and other stakeholders to promote practices, policies, and technology innovations across industry and government that address our shared climate challenges, particularly to reduce greenhouse gas emissions to the lowest levels possible at the pace of innovation.

Having been engaged on ESG topics across all industries, the Chamber is also a ready participant in conversations about the impacts of climate change on our financial system and believe there is much common ground on these issues. While the Chamber is supportive of the overall goals of the BCBS principles as we move toward a carbon-free economy, we also support the development of market-driven solutions to these problems. As we noted in a 2020 report, "the fundamental challenge we face today is to preserve the ability of our nation's companies to grow, innovate, and drive prosperity under a system of free and fair capitalism. The Chamber—through its Project Growth and Opportunity or "Project GO"—is committed to identifying practical, sustainable ways to address socio-economic challenges."[1]

As the BCBS pursues acting on these principles, it is important to understand the actions that U.S. regulators are pursuing regarding climate risk. The U.S. Office of the Comptroller of the Currency (OCC) is currently accepting comments on a proposal

[1] Restarting the Growth Engine: A Plan to Reform America's Capital Markets, U.S. Chamber of Commerce Center for Capital Markets Competitiveness (November 2020) ccmc_growthengine_final.pdf (uschamber.com)

it issued in late 2021 on climate-related financial risk management for large banks. As noted in that request, after it has thoroughly reviewed public comments, the OCC plans to issue forthcoming guidance on climate risk "that would distinguish roles and responsibilities of boards of directors (boards) and management, incorporate the feedback received on the principles, and consider lessons learned and best practices from the industry and other jurisdictions."[2] The Chamber is encouraged by the OCC's stated intention to incorporate feedback from stakeholders.

We urge the Basel Committee to work in conjunction with regulators in the U.S. who are taking these similar steps on climate risk to help increase efficiency and avoid duplicative and redundant recommendations and policies for banks.

The Committee's principles aim to "achieve a balance in improving practices related to the management of climate-related financial risks and providing a common baseline for internationally active banks and supervisors, while maintaining sufficient flexibility given the degree of heterogeneity and evolving practices in this area." The principles also urge banks to "consider the potential impacts of climate-related risk drivers on their individual business models and assess the financial materiality of these risks and note that "banks should manage climate-related financial risks in a manner that is proportionate to the nature, scale and complexity of their activities and the overall level of risk that each bank is willing to accept." The Chamber appreciates the Committee's consideration that banks must weigh financial materiality against their individual business models, as well as the recognition that banks have differing levels of scale and complexity, which greatly impacts the amount of risk a bank is willing to accept.

Below, we offer comments the principles and make recommendations that we feel could improve the safety and soundness of the global financial system as banks continue to address emerging and evolving climate risks.

II. Principles for the management of climate-related financial risks

Governance

Principles 1-3 highlight several recommendations for bank boards and management in managing climate-related financial risk. The principles note in general that bank management should have appropriate understanding of climate-related financial risk and should develop roles and responsibilities throughout its organizational structure. Determining what is "appropriate" is an important step for banks. In making this assessment, each bank should be able to use discretion to make

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[2] *Principles on Climate-Related Financial Risk for Large Banks*, Office of the Comptroller of the Currency https://www.occ.treas.gov/news-issuances/bulletins/2021/bulletin-2021-62a.pdf

those determinations based on their business models and overall risk strategies rather than having that level of appropriateness determined through these principles or jurisdictional supervisors. There is no fixed standard or definition of what is "appropriate" regarding a bank's understanding of climate risk, and banks will have differing approaches based on the size and complexity.

The principles also note that banks "should take material physical and transition risk drivers into consideration when developing and implementing their business strategies." Many banks are incorporating climate-related policies and responsibilities throughout their organizations, and there is no uniform way that banks are accomplishing this. As mentioned above, banks need the flexibility to determine what types of controls are adequate and should be allowed to incorporate them into their organizational structure in a way that best fits their business models. Further guidance from the Committee should demonstrate an appreciation for these actions currently being taken by banks and the deep understanding of climate risks that banks already possess.

Climate-related risk is one of a host of risks, and banks must institute different strategies to prepare for each type of risk in their strategic planning. Banks are already demonstrating a significant understanding of these risks and are integrating climate-related policies and responsibilities throughout their organizations. We urge the Committee in any future action to consider these efforts by banks and not to place an undue emphasis on climate-related risks over others in a bank's overall risk strategy.

Internal control framework

The principles note that frontline staff "should have sufficient awareness and understanding to identify potential climate-related financial risks" during client onboarding. While undertaking independent climate-related risk assessment as part of the risk function and performing regular reviews as part of the audit function are understandable, the Chamber is concerned about the level of expertise that is expected of frontline workers. What constitutes "sufficient awareness and understanding to identify potential climate-related financial risks?" In planning their overall risk strategies, it is important for banks to understand the level of training needed for frontline employees to have "sufficient awareness" and how this level of understanding compares to that of boards and management.

Capital and liquidity adequacy

The principles note that banks should account for material climate-related financial risks in their internal capital adequacy assessment process (ICAAP) and their internal liquidity adequacy assessment process (ILAAP) and notes that these risks will

probably be incorporated “iteratively and progressively, as the methodologies and data used to analyse these risks continue to mature over time and analytical gaps are addressed.” The principles also note that “banks should assess the links between climate-related financial risks and traditional financial risk types such as credit and liquidity risks.”

The Chamber is opposed to any forthcoming recommendations on climate-related financial risk that are designed or intended to shift capital away from industries or sectors that may have, or be perceived to have, more environmental risk. We urge the Committee not to recommend standards that would determine capital allocation. We believe such actions could be inherently subjective and outside the scope of BCBS's charter. We encourage the Committee to limit its focus to supporting banks in their assessment of climate risks only for safety and soundness purposes.

The principles mention that banks “should identify and quantify climate-related financial risks and incorporate those assessed as material over relevant time horizons into their internal capital and liquidity adequacy assessment processes.” Many banks are already incorporating these risks into their risk management profiles and are doing so over various time horizons. U.S.-based banks have already stringent capital and liquidity requirements, and their resiliency was demonstrated during the economic shock precipitated by the COVID-19 pandemic. The Chamber supports permitting flexibility for capital and liquidity requirements.

Comprehensive management of credit risk

The principles call on banks to consider whether “adjusting credit underwriting criteria, deploying targeted client engagement, or imposing loan limitations or restrictions such as shorter-tenor lending, lower loan-to-value limits or discounted asset valuations.” Banks already consider climate-related financial risk in credit decisions, but climate risks are part of a larger risk assessment. The Chamber is concerned about outsized weight being placed on climate risk as opposed to other risks that banks must consider when making credit decisions.

Comprehensive management of market, liquidity, operational and other risks

Banks also already account for how climate-related financial risks could affect liquidity buffers and incorporate these risks into their overall risk management profile. As noted above, with already stringent liquidity requirements in place for banks, the Chamber cautions the Committee against heightened liquidity requirements that could unnecessarily impair banks' ability to meet customer needs.

As with any new standards that may be implemented by jurisdictional supervisors, legal and compliance risks will increase for banks as they are required to incorporate climate risk into their overall risk profiles. This will be particularly acute for banks that have instituted a massive increase in legal and compliance staff in the wake of the significant increase in regulations following the worldwide financial crisis of 2007-08. The Chamber urges the Committee to weigh the implications of future actions regarding climate risk on banks' compliance efforts. Such compliance costs are regressive to the size of an institution. This is important to note as mid-size banks are important providers of financing for main street businesses.

Scenario analysis

The Committee also notes that "with regard to scenario analysis, including stress testing, the principles are formulated with a view towards application to large, internationally active banks and to supervisory and other relevant financial authorities in Basel Committee member jurisdictions. However, smaller banks and authorities in all jurisdictions can benefit from a structured consideration of the potential impact of climate-related financial risks."

The scenario analysis undertaken by banks is conducted in a multitude of ways, and banks have different measurements and goals behind the analysis based on their business models. Importantly, this scenario analysis is usually conducted over a longer time horizon and differs from traditional regulatory stress testing, which is more focused on near-term economic stress. The principles note that "the field of climate scenario analysis is highly dynamic, and practices are expected to evolve rapidly, especially as climate science advances. Climate scenario models, frameworks and results should be subject to challenge and regular review by a range of internal and/or external experts and independent functions." The Chamber agrees with the Committee's assessment that climate scenario analysis is relatively new and is rapidly changing. In fact, the term "scenario analysis" is somewhat ambiguous, as it could encompass many different types of planning and have a different meaning for each bank. Banks should be allowed flexibility to determine what scenario analysis means for them as they incorporate it into their risk management strategy. Regarding the review of climate scenario models by internal and external experts, and the advancement of climate science, it is important to note that climate science is evolving and that banks should be allowed latitude as they adjust to new scientific information.

Many banks are making investments in more climate-smart, modern, resilient infrastructure to reduce overall risks over the asset lifecycle. From a climate risk perspective, banks take into consideration the plausibility and certainty of a risk to determine materiality. Risks that meet these criteria will warrant greater attention by

boards and management. If a bank determines that risks are speculative and distant, they generally will not consider them material or give them heightened scrutiny.

It is important to reiterate that the Chamber does not believe that scenario analysis should in any way be tied to capital or liquidity requirements. Scenario analysis should only be used to help understand potential risks to a bank's balance sheet and inform its overall risk management strategy.

Any forthcoming recommendations related to climate-related financial risk should be made only after weighing the costs and benefits of the chosen course, with justification for new policies being made clear to affected parties and the public. Public notice and comment are a vital component of policymaking. Clear communication with banks is important, and banks should have fair and advanced notice of their disclosure and compliance obligations.

III. Principles for the supervision of climate-related financial risks

Responsibilities, powers and functions of supervisors

The principles urge supervisors of cross-border banking groups to share information and collaborate on climate risk resilience, as well as to engage a broad and diverse range of stakeholders to understand climate-related financial risk. In addition, supervisors are encouraged to use scenario analysis and to disclose the findings of any scenario analysis exercises, but importantly, to "take into account the level of uncertainty associated with scenarios when determining whether to disclose results." The principles correctly note that supervisors should acknowledge the limitations on scenario analysis and recognize that scenario analysis is highly dynamic and rapidly evolving. The Chamber appreciates this acknowledgment, as it is critical for banks who must plan risk over a variety of time horizons to have the ability to adapt to changing facts and circumstances.

The Chamber stands ready to work constructively with you on these issues going forward.

Sincerely,

Tom Quaadman
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Center for Capital Markets Competitiveness
U.S. Chamber of Commerce