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SUBMITTED ELECTRONICALLY AT <https://www.bis.org/bcbs/commentupload.htm>
Basel Committee on Banking Supervision
Centralbahnplatz 2
4051 Basel
Switzerland

Re: Comments on the Disclosure of Climate-related Financial Risks

To the Basel Committee on Banking Supervision (the “Committee”):

On behalf of the Natural Resources Defense Council (NRDC), we are pleased to submit these comments on the consultative document for the *Disclosure of climate-related financial risks*.

NRDC is an international nonprofit environmental organization with more than 3 million members and online activists. Since 1970, our lawyers, scientists, and other environmental specialists have worked to protect the world’s natural resources, public health, and environment. NRDC has offices in New York City, Washington D.C., Los Angeles, San Francisco, Chicago, Montana, New Delhi, and Beijing. Through its finance and legal experts, NRDC remains engaged in financial regulation and views sensible financial regulation as an integral part of mitigating climate change.

Bank disclosure of climate-related financial risk is pivotal for continuing to integrate this risk into banking supervisory and risk management frameworks. Currently, the Pillar 3 framework does not provide distinct or comparable information as to how climate risk drivers could impact a bank, the banking sector, and the broader banking system. As the consultative document states, “physical and transition risks can have wide-ranging impacts across sectors and geographies that result in financial risks to banks via micro- and macroeconomic transmission channels, potentially affecting the safety and soundness of banks and the stability of the broader banking system.”¹

The proposed requirements for quantitative and qualitative disclosures, in addition to providing important information to the market, can help ensure that banks begin to manage climate-related financial risks, and can provide guidance for supervisors to help them understand the specific ways in which climate risk can manifest as traditional

¹ Basel Committee on Banking Supervision, *Consultative document: Disclosure of climate-related financial risks*, Nov. 2023 (“Consultative Document”), 2.

financial risk. This would allow financial institutions to better manage their risks to ensure their operations, investment portfolios, and credit portfolios are protected.

Additional tools, such as transition plans where appropriate, and further refinements of existing methodologies, will help supervisors develop stronger approaches for incorporating climate-related financial risks into their oversight and assist banks in maintaining solvency and business continuity in the face of climate change.

Q1. What would be the benefits of a Pillar 3 disclosure framework for climate-related financial risks in terms of promoting comparability of banks' risk profiles within and across jurisdictions and promoting market discipline? What other benefits have been identified?

Q3. Would the Pillar 3 framework for climate-related financial risks help market participants understand the climate-related financial risk exposures of banks and how banks are managing these risks?

The integration of climate-related financial risks into the Pillar 3 disclosure framework is an essential part of the Basel III reforms and offers a transformative approach to how banks report and manage these risks. Benefits of integrating climate-related financial risks into the Pillar 3 disclosure framework include:

- Helping investors, depositors, and other market participants by requiring standardized reporting that allows banks to be compared as to their relative climate risk exposure.
- Helping banks by requiring transparent climate risk disclosure and motivating better climate risk management.
- Helping bank supervisors by giving them more information about individual banks and thus facilitating their regulatory oversight to ensure financial stability.

The move towards standardized reporting under this framework empowers stakeholders to make more informed decisions regarding their investments or deposits. It will allow them to compare the climate risk profiles and mitigation strategies employed by the different banks, not just within a single country but globally. By making banks more accountable to their shareholders, customers, and the community at large in the face of climate-related threats, these disclosure requirements should encourage banks to refine their risk management protocols and adopt practices to safeguard against climate-related vulnerabilities. This can help protect individual banks against climate-related financial risk, as well as contributing to a more stable financial system.

Finally, by providing increased transparency into the practices of individual banks, the framework allows regulatory authorities to better monitor and evaluate the financial system's resilience against climate-related threats. This oversight capability is crucial to creating regulatory policies and supervisory techniques that address systemic climate-related financial risk.

Q2. What are the risks of a Pillar 3 disclosure framework for climate-related financial risks not being introduced?

Failing to implement such a framework would allow financial institutions' unquantified climate risks to continue to develop in relative obscurity. This lack of clarity can result in misinformed decision-making and diminish accountability across the board. As noted in the consultative document, "[d]isclosure requirements are a fundamental component of a sound banking system, as providing market participants with meaningful information . . . reduces information asymmetry and promotes comparability of banks' risk profiles within and across jurisdictions."²

Without mandated disclosures, banks have less incentive to incorporate climate-related considerations into their risk management strategies, leaving them ill-prepared for the financial ramifications of climate change. This scenario not only exposes individual institutions to potentially significant financial losses but also escalates systemic risk, given the interconnected nature of the financial system. The failure of one bank due to unaddressed climate risks could trigger a domino effect, impacting the broader financial landscape. The erosion of market discipline reduces the market incentives for banks to adopt prudent risk management practices, weakening the overall market's health. Failure to disclose and manage their climate-related risk exposures also can cause severe reputational damage for banks, potentially eroding customer trust and investor confidence, which are crucial for maintaining market value and a stable customer base.

In essence, eschewing a Pillar 3 disclosure framework that addresses climate-related financial risks not only poses financial and operational hazards to banks but also amplifies systemic vulnerabilities, and risks the integrity and stability of the financial sector.

Q4. Would the Pillar 3 framework for climate-related financial risks be sufficiently interoperable with the requirements of other standard-setting bodies? If not, how could this best be achieved?

Per the consultative document, the Committee has been "closely monitoring the development of global frameworks to improve the consistency, comparability and reliability of climate disclosures. It has also been coordinating with other international bodies and standard setters, including the International Sustainability Standards Board (ISSB), as it explores use of Pillar 3 of the Basel Framework to promote a common disclosure baseline for climate-related financial risks across internationally active banks."³ We highly commend the Committee's consideration of interoperability of the climate disclosure framework with the ISSB. The standards formulated by the ISSB (IFRS S1 and S2) have been translated into local regulatory requirements across jurisdictions including the United Kingdom, Japan, Brazil, Canada, Singapore, and South Korea. Aligning the Pillar 3

² Consultative Document at 1.

³ Consultative Document at 1.

framework with the recommendations of the ISSB is critical to promoting consistency, comparability, and reliability of disclosure standards for market participants.

Q5. Would there be any unintended consequences of a Pillar 3 framework for climate-related financial risks? If so, how could these be overcome?

Implementing a Pillar 3 disclosure framework for climate-related financial risks is a step towards greater transparency and stability in the financial system, but there is a real danger that the adoption of enhanced climate risk mitigation measures by banks may disproportionately affect climate-burdened communities, including lower-income communities and communities of color. We urge the Committee to consider additional research and guidance to address likely effects on these communities.

A substantial and growing literature demonstrates that many climate-related risks, such as the risk of weather-induced hazard or sea level rise, are likely to be disproportionately borne by lower income communities and communities of color.⁴ Of particular concern are risk mitigation measures that force individual households and small businesses to internalize climate-related risks without providing solutions to reduce their risk. Mitigation options like imposing loan restrictions or limiting exposure to certain geographic regions could have this effect. Such measures may significantly restrict access to credit within already disadvantaged communities, further reducing their capacity to respond to climate-related challenges such as weather-related disasters or sea level rise. NRDC recommends that banks and their regulators evaluate a broad range of mitigation options and prioritize options that do not restrict fair access to credit for disadvantaged communities.

The wider implications of implementing a disclosure framework need careful consideration. Banking regulators should be urged to engage with a broad spectrum of stakeholders within their jurisdictions to help identify and mitigate potential adverse impacts. Bank regulators should require banks to take steps to avoid potential disproportionate impact on banking customers in disadvantaged communities as they formulate climate risk mitigation measures. Going beyond this, jurisdictions should take a whole-of-government approach that marshals public and private resources to mitigate the disproportionate impact of climate change on such communities, including any potential reductions in lending because of climate risk. By thoughtfully addressing these potential unintended consequences, the Pillar 3 disclosure framework can contribute to a more transparent, resilient, and inclusive financial system that supports the global transition to sustainability.

⁴ See, e.g., Buchanan, Maya K., Scott Kulp, Lara Cushing, Rachel Morello-Frosch, Todd Nedwick, and Benjamin Strauss, "Sea Level Rise and Coastal Flooding Threaten Affordable Housing", *Environmental Research Letters* 15, no. 12 (2020): 124020; Keenan, Jesse, and Elizabeth Mattiuzzi, "Climate Adaptation Investment and the Community Reinvestment Act", *Community Development Research Brief* 05 (2019): 01-30; Furman Center, *Population in the U.S. Floodplains*, https://furmancenter.org/files/Floodplain_PopulationBrief_12DEC2017.pdf

Q11. What are the benefits of the proposed qualitative Pillar 3 climate-related financial risk disclosure requirements?

The qualitative climate-related disclosure requirements—governance, strategy, risk management, and concentration—have the virtue of requiring banks to disclose publicly how they are thinking about climate change in regard to their business. The requirements address process (governance and risk management), climate exposure (risk management and concentration), and intended actions (strategy).

Based on these qualitative disclosures, a bank’s stakeholders, including current and potential investors, depositors, and regulators, can assess the bank’s attentiveness to climate risk and compare it to that of other banks. In addition to providing this important information to the market, the prospect of being required to make these disclosures creates an incentive for the bank to address climate risk seriously or run the risk of unfavorable comparison with its peers.

Of course, by their nature, qualitative disclosures are imprecise and vulnerable to “greenwashing”: for example, broad unverifiable assertions about climate-related activities that are not backed up by efficacious actions. For this reason, these disclosures must be closely monitored by bank regulators and coupled with appropriate quantitative disclosures. But the qualitative disclosure requirements described in the consultation paper nevertheless can play an important role in providing useful information to the market and bank regulators, while providing a positive incentive to the bank.

The consultation paper refers to banks’ transition plans. Banks should be encouraged—or even required—to use and disclose transition plans when they have made net-zero commitments. Transition plans are essential to understand banks’ climate strategy, targets, and decarbonization accomplishments to date, and, based on these, to assess whether banks are in the position to manage their climate-related risks. Disclosing a transition plan within a climate disclosure framework significantly enhances a company’s approach to managing and communicating its strategies for adapting to a low-carbon economy.

Recently, the U.S. Treasury Department published principles that lay out best practices for banks that have made or are considering making net-zero commitments.⁵ A key element of these principles is the development of transition plans. Transition plans translate an institution’s net-zero commitment into specific objectives and actions that are aimed at reducing real-economy GHG emissions, providing credibility and accountability to net-zero commitments. They help set shared expectations and goals for net-zero commitments between the institution, its clients, and the regulating bodies. This level of detail is invaluable for stakeholders to gauge a company’s commitment and effectiveness in navigating the transition and maintaining financial stability.

⁵ *Principles for Net-Zero Financing & Investment*, US Department of the Treasury (Sept. 2023), <https://home.treasury.gov/system/files/136/NetZeroPrinciples.pdf>

A forward-looking approach and a long-term view are essential when addressing climate-related financial risks. The disclosure framework should mention transition plans as a tool to help supervisors understand and oversee climate-related financial risks in a forward-looking manner for those banks with net-zero commitments. Financial supervisors have already recognized the role of transition plans as a source of information and a possible supervisory tool. It is important that supervisors also recognize the 2050 net-zero emissions horizon established in the Paris Agreement objectives (2050) as a common anchor point for transition planning. Supervisors should then assess whether banks have set appropriate climate targets, including intermediate targets, and whether they are reaching those targets to mitigate relevant risks.

Moreover, when creating and disclosing transition plans, institutions should identify sustainability issues that are significant both from the perspective of their potential financial impact and their societal or environmental implications. Reporting requirements under the EU's Corporate Sustainability Reporting Directive (CSRD) came into effect in January 2024 requires companies to apply such thinking to identify their required climate change disclosures.

Q17. What are the benefits of the proposed quantitative Pillar 3 climate-related financial risk disclosure requirements?

The disclosure of financed and facilitated emissions, including Scope 1 (direct emissions from owned or controlled sources), Scope 2 (indirect emissions from the generation of purchased energy), and Scope 3 (all other indirect emissions that occur in a company's value chain), along with off-balance sheet items, is crucial for fostering transparency and accountability in the fight against climate change. By providing a comprehensive view of an organization's carbon footprint, including emissions associated with financial activities and investments, stakeholders are better equipped to assess the climate-related risks of banking operations and strategic decisions. This level of disclosure empowers investors, consumers, and regulatory bodies to make informed choices. The Committee should work further with supervisors to establish a uniform understanding, definitions, and methodologies for climate-related financial risk metrics.

Q52. What are your views on the feasibility of the potential effective date of the Pillar 3 climate-related disclosure requirements?

Q53. Would any transitional arrangements be required? If so, for which elements and why?

The Committee should establish a climate risk disclosure framework as soon as possible, given the escalating risks climate change poses to financial stability and the urgent need for transparency in how financial institutions are exposed to and managing these risks. As banks play a pivotal role in allocating capital across the economy, their actions can

significantly exacerbate the financial system’s vulnerability to climate-related shocks, threatening economic stability and the well-being of communities worldwide.

To ensure timely progress, we propose phasing in the climate disclosure framework, starting with qualitative disclosures to be required as soon as practicable, followed by quantitative disclosures at a later stage to allow time for gathering and calculation of required data. It’s important to recognize that this will be an iterative process, and that initial imperfections should not deter progress. The pursuit of perfection should not overshadow the importance of making good, progressive steps forward, even if they are not flawless from the outset.

Q54. What are your views on the Committee exploring disclosure requirements for the impacts of climate-related financial risks on deposits/funding and liabilities?

As the Committee has noted, climate-related financial risks may materialize through traditional risk categories, including liquidity risk. In particular, the Committee has recognized that climate-related financial risks could include net cash outflows, depletion of liquidity buffers, and/or decreases in value of assets comprising such buffers, and should, when material, be considered in banks’ internal liquidity assessments, calibration of liquidity buffers, and liquidity risk management frameworks. Therefore, requiring disclosure of climate-related financial risks to deposits/funding and liabilities is critical for banking risk management. Because liquidity risks are likely to vary by sector and geography, the disclosures should include sector and geographic detail similar to the proposed templates.

In the United States, for example, long-term mortgages are bank assets that are traditionally paired with annually renewed homeowner insurance policies. A repricing of, or failure to renew, those insurance policies as insurers price in the risk of acute climate events (as we are seeing already in several regions⁶) may increase the cost of homeownership, or lead to borrowers dropping homeowner insurance altogether, can result in serious financial implications for borrowers, leading to delinquencies and defaults on a critical scale and affecting property values in climate-exposed areas. Banks with balance sheets subject to the related credit and market risks could find themselves unable to refinance in the short term.

Climate-related financial disclosures are crucial in today’s landscape, serving as a key component in assessing and managing the risks—and opportunities—presented by

⁶ See, for example, Ryan Mac, “Allstate Is No Longer Offering New Policies in California”, N.Y. Times, June 4, 2023, <https://www.nytimes.com/2023/06/04/business/allstate-insurance-california.html>; Christopher Flavelle, Jill Cowan and Ivan Penn, “Climate Shocks Are Making Parts of America Uninsurable. It Just Got Worse”, N.Y. Times, May 31, 2023 (updated June 2, 2023), <https://www.nytimes.com/2023/05/31/climate/climate-change-insurance-wildfires-california.html>; Mahsa Saeidi, “3 insurance companies stop or limit writing new business in Florida”, WFLA News Channel 8, May 31, 2022 (updated June 1, 2022), <https://www.wfla.com/8-on-your-side/3-insurance-companies-stop-or-limit-writing-new-business-in-florida/>

climate change. These disclosures enable banks to provide transparent information regarding their exposure to climate-related risks. By offering a clear view of how climate change affects banking operations and financial performance, these disclosures help regulators ensure the financial safety and soundness of the individual banks and the global financial system.

We thank the Committee for its consideration of our comments. If we can be of any further assistance, please do not hesitate to contact us.

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