American Bankers Association
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Electronically delivered
Ann Misback
Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue
Washington, DC 20551

Re: Principles for Climate-Related Financial Risk Management for Large Financial Institutions; Docket No OP-1793

Dear Ms. Misback:

The American Bankers Association[1] appreciates the opportunity to provide feedback on the *Principles for Climate-Related Financial Risk Management for Large Financial Institutions* ("the Principles") published for comment by the Federal Reserve. The Principles intend to improve the identification and management of climate-related financial risks at banking organizations with $100 billion in assets and above. The Principles call for enhanced governance, strategic planning, risk management, oversight, and data reporting practices for climate-related financial risks, and largely mirror those previously issued by the Basel Committee on Banking Supervision (BCBS), the FDIC and OCC.

ABA and its members reiterate our understanding that climate change has implications for banking organizations, their counterparties and the communities banking organizations serve.[2] Overall, we continue to support the Principles as a high-level guide for the largest institutions, but are concerned about the process through which the Principles are being developed. Additionally, given the level of complexity and uncertainty related to identifying and measuring climate-related financial risk, we recommend that before finalizing the Principles, the Federal Reserve work with the FDIC and OCC to clarify and make consistent the definitions of key terms and concepts.

As a threshold matter, we urge the Federal Reserve, together with the FDIC and OCC, to maintain a robust and transparent process when developing climate-related financial risk guidance or rulemakings in the U.S. The Principles are based on those developed by the BCBS, which were finalized in June

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[1] The American Bankers Association is the voice of the nation's $23.3 trillion banking industry, which is composed of small, regional and large banks that together employ more than 2 million people, safeguard $19.2 trillion in deposits and extend nearly $11 trillion in loans.
[2] ABA has developed a set of principles guiding our advocacy on these issues: https://www.aba.com/advocacy/policy-analysis/climate-change-and-banking

2022[3] and largely mirror those proposed by the FDIC and OCC earlier this year.[4] It seems that the Federal Reserve is advancing concepts finalized by the BCBS, such as the directives for institutions to (1) analyze and possibly change their compensation policies and (2) include "measures of conservatism," in risk management and controls.[5] Neither of the these factors were included in the FDIC's or OCC proposed principles, but are in the final BCBS Principles and Frequently Asked Questions (FAQ),[6] issued subsequent to the proposals by the OCC and FDIC. Basing U.S. policy proposals on final Basel Committee documents implies that these concepts are already accepted and embedded in the Basel framework, and thus not actually open for comment for purposes of U.S. implementation.

Going forward, we urge the Federal Reserve, together with the FDIC and OCC, to seek early and frequent public input when developing standards through international bodies. Once finalized, internationally developed guidance and standards, such as the BCBS Principles, may alter the provision of financial services to certain industries and communities. The economic effects of this will be felt by all banks, which will need to adapt to the resulting market changes and ensure that financial services to vulnerable communities and customers are preserved. It is incumbent on the banking agencies to ensure that all banks have sufficient opportunity to provide comments on potential policy decisions. Feedback from a wide variety of stakeholders will help ensure that international standards are properly calibrated to U.S. laws and markets and do not harm the customers and communities banking organizations serve. Additionally, we respectfully note that central banks and supervisors in other jurisdictions may have broader mandates than the Federal Reserve or other U.S. regulators do, so that not all international standards or parts thereof would be appropriate for U.S. implementation.

Climate-Related Guidance Should Remain High Level and Flexible

As the Federal Reserve is aware, the industry is currently working to better understand its climate-related risks and communicate the information and actions to regulators, investors and other stakeholders. As the Federal Reserve is also aware, defining and quantifying climate related impacts is a new and complex process with limited data and nascent methodologies that use timeframes well beyond what banking organizations typically consider. Moreover, the assumptions that back the analyses are dependent on a vast number of future policy outcomes, technological developments, and investment and lending opportunities that are by definition currently unknown. Given both the lack of data and the significant uncertainties surrounding climate-related financial risk assessment, we urge the Federal Reserve to continue to take a principles-based approach that is flexible and iterative. This will allow large banks to assess the risks they identify as the most material to their unique circumstances. Additionally, this approach will allow banks to incorporate changes to their methodologies as they develop, and the policy and economic trajectories become clearer.

To that end, ABA and its members support the Proposal's flexibility in permitting climate-related financial risks to be incorporated into existing risk types. Climate-related financial risk may be most effectively managed within existing risk management frameworks, which already account for climate-related financial risk. The Proposal acknowledges that existing corporate governance and risk

[3] Principles for the effective management and supervision of climate-related financial risks, BCBS. June 2022

[4] FDIC: 87 FR 19507. Pages 19507-19512, (June 3, 2022); OCC: Principles for Climate-Related Financial Risk Management for Large Banks, December 16, 2021

[5] Ibid. BCBS Principles, June 2022.

[6] Frequently asked questions on climate related financial risks, BCBS. December 2022.

management standards applicable to banking organizations are sufficient and flexible enough to accommodate climate-related financial risks. We believe that the final guidance should retain this flexibility.

Additionally, we support the Principles' recognition that organizations should tailor risk-management practices to the nature, scope, and risk of their activities. Consistent with the Federal Reserve's existing supervisory framework,[7] we recommend that the Principles further address the possibility that climate-risk management practices may differ not only among supervised organizations, but also within an organization's different operations or lines of business. Incorporating this into the Principles would complement the Federal Reserve's risk-based approach by enabling organizations to tailor their risk management practices to address the unique risks presented by different activities, including those by both banking and nonbanking operations or lines of business. We also recommend that the Principles make clear that the Federal Reserve intends to rely to the fullest extent possible on the supervisory work of other functional regulators.

We agree with Governor Bowman that if finalized, the Principles should "complement the existing supervisory framework supporting the safety and soundness of financial institutions, and that the Board consider the costs and benefits of any new expectations." [8]Further, we appreciate the comments of Governor Waller, and agree that climate-related financial risk is already embedded in banks' risk management framework.

It is Too Early to Expect Banking Organizations to Set Lending or Other Risk limits

We are opposed to provisions in the guidance that could be interpreted as requiring banks to adopt lending limits related to climate-related financial risk regardless of materiality. The Proposal suggests that "[m]anagement should incorporate climate-related financial risks into policies, procedures, and limits to provide detailed guidance on the financial institution's approach to these risks in line with the strategy and risk appetite set by the board." Mandating new lending limits specific to climate-related financial risk would be inconsistent with the regulatory expectation that banks' climate risk management framework include all material risk considerations to the bank.

We also caution against overly prescriptive board and management requirements, especially those that would require the board and management to go beyond their role on the subject of climate-related risk. We are concerned that several of the requirements in the proposal are overly prescriptive for the board or management and may limit a bank's ability to design and develop practices to address climate-related financial and other risks. For example, we are opposed to the Proposal's statement that a banking organization's board "should consider" changes to its compensation policies based on climate-related financial risk management practices, as well the Proposal's statement that the board "should assure" that public statements on climate-related strategies and commitments are consistent with strategies and risk appetites.

With respect to other financial risks, the Proposal indicates that management should include "corresponding **measures of conservatism**" in their measurements and controls. We recommend that the Federal Reserve not adopt this approach. The concept of "conservatism" often is understood within an outdated accounting concept that arbitrarily leans toward a worst-case scenario, rather than a

[7] *See, e.g.*, Federal Reserve Supervision and Regulation Letter 22-8: Framework for Supervision of Insurance Organizations.
[8] Statement of Governor Bowman, Statement of Governor Waller, Federal Reserve Board Meeting, December 2, 2022.

measurement that considers all plausible scenarios. As a result, applying such "measures of conservatism" can significantly depart from risk and capital management practices used throughout the institution. From the perspective of pricing risk, however, conservatism can unintentionally put LMI borrowers and at-risk communities at a disadvantage, and additionally would also likely discourage the financing new and emerging renewable energy technologies and infrastructure.

Provide Additional Clarity on Application to FBOs

More clarity is needed regarding the application of the Principles to the U.S. operations of foreign banking organizations (FBOs) to reflect the governance specificities for how FBOs operate and manage risk in the United States. The Federal Reserve should recognize that climate-related financial risk management is often an enterprise-wide effort that is routinely developed and coordinated at the home office or group-level. FBOs should be able to leverage existing risk management frameworks such as home office or group-level programs, policies, and procedures to comply with U.S. requirements. For example, many FBOs conduct exploratory climate scenario analysis exercises at the enterprise level to inform their global risk management frameworks. Boards should be able to rely on designated U.S. committees (e.g., a U.S. risk committee, or other relevant entity) regarding the board oversight of climate-related financial risks in the United States. FBOs should also be able to rely on U.S.-based management for relevant U.S. climate-related financial risk obligations for senior management. In addition, as written, it is unclear-how the final guidance would apply to FBOs; the final guidance should clarify that the principles apply to FBOs in a consistent manner based on the size of their combined U.S. operations.

Ensure the Principles Are not Applied to Community Banks

We do not believe that the Principles are appropriate for smaller institutions and urge the Federal Reserve to work with the OCC and FDIC to ensure it does not trickle down through the supervisory process.

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The legal, regulatory and supervisory framework that governs U.S. banking organizations is among the world's deepest and strongest. Moreover, banks are well-practiced in adapting to and managing change in the business environment and consumer and market preferences. Climate-related financial risks are naturally embedded into banks' risk management processes through the dynamic market, economic, and counterparty data that are the backbone of risk management. As the policy goals, definitions, and methodologies behind climate-related financial risk identification evolve, banks of all sizes will continue to apply traditional credit and financial risk tolerances and parameters to their balance sheets to manage their risks and support the customers and communities they serve.

If you have any questions about these comments, please contact the undersigned at (202) 663-5182 or email: atouhey@aba.com.

Sincerely,

Alison Touhey