The Honorable Randal Quarles
Vice Chair of Supervision
Federal Reserve System

The Honorable Jelena McWilliams
Chairman
Federal Deposit Insurance Corporation

The Honorable Todd Harper
Chairman
National Credit Union Administration

Michael Hsu
Acting Comptroller of the Currency
Department of the Treasury

September 29, 2021

Dear Vice Chair Quarles, Chairman McWilliams, Chairman Harper, and Comptroller Hsu:

We are writing to call on you to promptly take steps to address climate risk to individual banks, bank holding companies, and credit unions (collectively, banks) under your jurisdiction. Recent climate science reports have further confirmed the link between climate change and the increasing frequency and severity of physical disasters, which can pose risks to banks. The European Central Bank's preliminary findings from its own supervisory review, for example, show that most of its banks are not prepared for climate impacts today, much less the greater threats of tomorrow. To address these developing threats, we encourage you—and your bank examiners—to incorporate climate risk into your agency's regular examinations. As an immediate step, we encourage you to issue supervisory guidance detailing specific issues that banks and your examiners will be expected to consider, measure, and evaluate.

Your examiners routinely review the assets and practices of the institutions they regulate to, at minimum, identify banks' activities or assets that are "unsafe or unsound"[1] and may place the institutions and the banking system at undue risk.[2] They may direct banks to stop those risky activities, divest those risky assets, and otherwise bring their lending activities in line with regulators' expectations. In addition, examinations allow supervisors to learn about banks' activities and collect data about the industry as a whole. Bank regulators routinely issue supervisory guidance that identifies the types of activities that may be unduly risky or may create contagion and systemic risk, and provide banks with expectations on mitigating those risks.

Examiners regularly assess credit risk, market risk, liquidity risk, and operational risk. Each of these risks (and others) are implicated by climate change. Banks face exposure to climate-related risks from acute and chronic physical damages and productivity losses (physical risk) as well as from the ongoing transition away from high carbon industries driven by regulation, technology, consumer preferences, and growing legal liability (transition risk). It is part of your mandate as

[1] See e.g., 12 U.S.C. § 1818. See also *id.* § 1844(c)(2).
[2] The failure of banks that engage in overly risky activities can result in significant harms that propagate into the real economy. Although Congress has enacted laws to rein in the excesses of the banking industry, regulators are expected to examine their institutions at least every 18 months to ensure compliance. 12 U.S.C. §§ 1820(d), 1756.

prudential regulators to incorporate climate risk into your assessments, much as you consider any other bank-specific and systemic risks when analyzing, for example, improper credit risk management or concentration issues.[3]

It is urgent that you begin examining banks for climate-related risks and make sure they are aware of the potential consequences of not adapting their activities to these risks. You must promptly provide specific guidance to banks that discusses both the physical and transition risks of climate change; details specific issues that examiners will consider, measure, and evaluate; and provides banks with clear expectations.[4] We have attached an explanation of how climate change creates credit risk, market risk, liquidity risk, and operational risk to financial institutions, which we encourage you to incorporate into your supervisory guidance.

Issuing clear guidance for banks and examiners on expectations for climate-related risk exposure is a necessary first step regulators must take: one that many banking regulators around the world have already implemented[5] and have found in doing so that banks are falling short on prudent climate risk management.[6]

We would be pleased to speak with you or members of your staff or assist in other ways to help you expeditiously achieve this goal.

Sincerely,

Americans for Financial Reform Education Fund
Center for American Progress
Friends of the Earth US
Public Citizen
Natural Resources Defense Council
Sierra Club

cc: The Honorable Janet Yellen, Treasury Secretary

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[3] See e.g., Bank Holding Company Supervision Manual § 2010.2 (Jan. 2015 ed.), https://www.federalreserve.gov/publications/files/bhc-2000-201709.pdf

[4] Because supervisory guidance is rarely one-size-fits-all, we encourage you each to tailor your guidance to the institutions you supervise. Bank holding companies face risks that are significantly different from those faced by many community banks and credit unions.

[5] *See e.g.*, Bank of England, Enhancing Banks' and Insurers' Approaches to Managing the Financial Risks from Climate Change, Supervisory Statement 3/19 (Apr. 2019), https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/supervisory-statement/2019/ss319.pdf; European Central Bank, Guide on Climate-Related and Environmental Risks: Supervisory Expectations Relating to Risk Management and Disclosure (Nov. 2020), https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm.202011finalguideonclimate-relatedandenvironmentalrisks~58213f6564.en.pdf.

[6] European Central Bank, *The Clock is Ticking for Banks to Manage Climate and Environmental Risks* (Aug. 18, 2021), https://www.bankingsupervision.europa.eu/press/publications/newsletter/2021/html/ssm.nl210818_5.en.html.