June 30, 2022

Delivered Via Email: fsb@fsb.org

Klaas Knot
Chair
Financial Stability Board Bank for International Settlements CH-4002 Basel, Switzerland

Re: Supervisory and Regulatory Approaches to Climate-Related Risks

Dear Chairman Knot:

World Council appreciates the opportunity to comment on the Financial Stability Board’s (FSB) consultative report on the Supervisory and Regulatory Approaches to Climate-Related Risks: Interim Report. Credit unions are cooperative depository institutions and World Council is the leading trade association and development organization for the international credit union movement. Worldwide, there are over 86,000 credit unions in 118 countries with USD 3.2 trillion in total assets serving 375 million physical person members.

World Council supports the FSB’s goal to create a consistent global approach to addressing climate-related risks, specifically the consideration of proportionality based on the consideration of the nature, size, and risk profile of a financial institution. While we support the objectives stated within the report, we urge the FSB to further consider the impact of their recommendations on smaller community-based financial institutions such as credit unions and cooperatives. World Council asks that the FSB provide definitive instruction to national-level regulators to implement proportional requirements, clearly define or characterize risk terms and the materiality threshold, and provide guidance on how to apply its recommendations proportionately.

World Council’s responses to FSB’s questions are below (some responses have been omitted based on applicability):

3. Does the report appropriately identify the elements of a common high-level definition of climate-related risks (physical, transition and liability risks)?

While the report does identify the elements of common high-level definitions of climate related risks and the metrics some jurisdictions are using to define them, with regards to proportionality they are broadly presented. We urge the FSB to further define these risks to avoid confusion,

1 Public consultation on FSB’s Supervisory and Regulatory Approaches to Climate-related Risks, see: https://www.fsb.org/wp-content/uploads/P290422.pdf.
over inclusiveness, and inconsistency. Leaving authorities across jurisdictions to define physical, transition and liability risk could be detrimental to small financial institutions such as credit unions. For example, the report diverges into several lanes with respect to the definition of liability risk, stating that, “Some national authorities have accounted for liability risk within their definitions of either physical or transition risks, while others have established separate definitions for liability risk as an additional risk. Others have accounted for liability risk more broadly as ESG factors. However, liability risk might materialise independently from transition risks and far in advance from the materialisation of both transition and physical risks.” This lack of clarity, coinciding with requirements from other standard setting and international bodies can cause unnecessary regulatory burden. For instance, with the IFRS moving towards new standards in sustainable finance, including additional disclosures for ESG and other climate-related matters, it is especially taxing on small financial institutions to collect, analyze, and determine what climate-related data is applicable for who and when. The FSB’s breakdown of qualitative and quantitative data is especially helpful, and leaves less room for interpretation, which helps financial institutions identify what they can and cannot accomplish in terms of data reporting to applicable supervisory authorities. Its specificity is welcome across all recommendations.

We further urge the FSB to consider baseline risk definitions with clear direction to authorities to include proportionality language while allowing authorities the flexibility to expand upon these terms for larger financial institutions. We also ask for clear proportional guidance to authorities as to how to practically apply their risk reporting requirements in a way that considers the nature, size, and risk profile of a financial institution. Without defined and proportional guidance, national-level regulators are free to impose strict, overly burdensome requirements that may be impossible for credit unions to comply with.

4. Do the proposed recommendations help accelerate the identification of authorities’ climate-related information needs from financial institutions and work towards common regulatory reporting frameworks? Please elaborate on areas where the recommendations could be enhanced, if any. Incorporating systemic risks into supervisory and regulatory approaches

Identifying informational needs, supervisory oversight over governance, processes, and controls, third-party data verification, and common definitions for physical risk, transition risk, and liability risk are appropriate recommendations, but may prove onerous for credit unions, especially if authorities tailor these requirements to fit large financial institutions and G-SIBs. Further, recommending that authorities ask financial institutions to report qualitative and quantitative information to supervisors in addition to higher reporting standards and/or mandatory reporting requirements could be a serious impediment to credit unions.

Additional compliance burdens, even those that are less demanding, can be extremely difficult for credit unions and smaller financial institutions to implement. They often do not have the resources necessary to comply with increased regulation. It is necessary that the FSB provide authorities with guidance on how to provide either exceptions or proportional reporting requirements. Oftentimes, credit unions are the weakest offenders as it relates to climate-related concerns and employing overly burdensome regulation for credit unions is counterproductive to the goals of climate change. Clearly defined proportional language within the recommendations is necessary to allow credit unions to function, and to use their small
margins of revenue to service their members that are often part of underserved and underbanked communities.

Additionally, the recommendations fail to include the threshold of materiality. While the report as a whole addresses materiality, the recommendations not only fail to specify the inclusion of materiality when determining risk, identifying informational needs, applying additional reporting requirements related to higher reporting standards as data improves, and providing qualitative and quantitative analysis, but it also misses the opportunity to characterize materiality. While it is understandable that the FSB would like to leave some flexibility to authorities across jurisdictions, some guidance on the materiality threshold is necessary to prevent confusion and inconsistency across jurisdictions, ultimately creating more regulatory and compliance burden for all financial institutions. This defeats the purpose of addressing climate-related risks and creating consistent global regulation to address these risks. The FSB does recommend collaboration between authorities across jurisdictions, however, the success or even the act of collaboration is not guaranteed to take place or even ensure that cooperation is comprehensive and effective. Examples of scenarios that rise to the level of ‘material’ would be valuable.

The report states that, “As authorities continue to evaluate their information needs beyond ad-hoc means and move towards regular standardised regulatory reporting requirements, key policy considerations include expansion of regulatory returns to gather more granular and specific climate-related data (such as for physical and transition risks) on a regular basis, capacity building, information technology capabilities and proportionality of requirements.” Again, World Council welcomes the inclusion proportionality within its recommendations, however, more specificity is welcomed. This statement significantly increases regulatory burden by promoting more data reporting on a “regular basis”. We urge the FSB to recommend clear guidance that states that a proportional approach is necessary, but just as importantly, identifies specific direction as to what steps are necessary to achieve proportionality including capital requirements, exemptions, thresholds and other necessary steps necessary to address the identified risks once risks are identified.

Furthermore, we are concerned that the amount of analysis necessary and the granularity that may be required by authorities may outweigh any benefit received by identifying reportable risks. It is vital that the regulatory burdens that stem from these recommendations do not disproportionately and unduly burden smaller financial institutions with limited resources. Recommendations such as these require further guidance as to how often, how granular, and how specific climate data should be for smaller financial institutions, otherwise it is likely that no proportionality will be used at all, as the focus of most financial regulation is on large banks. Again, the issue of what is material would likely cut down on the amount of reportable data, and most likely will remove some reporting requirements for credit unions because many of these institutions are not substantial contributors to climate issues such as emissions.

9. Are there any other issues that should be considered in future work of the FSB on supervisory and regulatory approaches to climate-related risks?

- The FSBs objectives to support financial inclusion and the challenges effecting financially excluded and underserved groups were not communicated within the report. While utilization of proportionality was suggested, the FSBs mission to expand access
to financial services and to address the unintended consequences of regulatory reform was omitted. We believe reference to this issue is critical and emphasizes the necessity of proportionality. Unfortunately, it is not enough to support proportionality. Authorities need clearly defined guidance as to how to apply it, and clear and convincing language recommending its application. The is a great risk that national-level regulators will only create standards tailored for G-SIBs and large financial institutions, leaving smaller financial institutions to weigh between applying revenue toward regulatory requirements, or keeping their institution afloat.

- Third-party verification mechanisms could prove costly for credit unions. We appeal to the FSB to recommend this option only for G-SIBs and large financial institutions.

- We ask the FSB to provide more guidance on granular data. For example, how granular should the data be? How do we weigh granular data with materiality? Does the risk analysis include third parties?

World Council appreciates the Financial Stability Board’s efforts to address climate-related risks and the consistency of reporting requirements across jurisdictions. If you have questions about our comments, please feel free to contact me at pmonford@woccu.org or +1-202-510-9347.

Sincerely,

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World Council of Credit Unions