BASEL COMMITTEE ON BANKING SUPERVISION – DISCLOSURE OF CLIMATE-RELATED FINANCIAL RISKS

E3G RESPONSE

14 March 2024

About E3G

E3G is an independent climate change think tank with a global outlook. We work on the frontier of the climate landscape, tackling the barriers and advancing the solutions to a safe climate. Our goal is to translate climate politics, economics and policies into action.

E3G builds broad-based coalitions to deliver a safe climate, working closely with like-minded partners in government, politics, civil society, science, the media, public interest foundations and elsewhere to leverage change.

Introduction and General Feedback (questions 1-10)

We are pleased to provide a written submission to the Basel Committee's consultation on disclosure of climate-related financial risks.

E3G strongly supports the holistic review of the global prudential framework currently conducted by the Basel Committee, and welcomes the consideration given by the Basel Committee to updated Pillar 3 prudential disclosure standards that would account for disclosure of climate-related financial risks.

The changes considered by the Basel Committee would help address the need for a pivot from voluntary action to regulation to secure financial system resilience and market integrity in the face of intensifying climate impacts. The Financial Stability Board **indicated in July 2021** that the Basel Committee was "assessing the materiality of gaps in the existing Basel framework" against climate-related risk, and would "consider the need for regulatory measures to address climate-related financial risk", by the end of 2024. While the Basel Committee has confirmed that this work is ongoing (including in the context of this draft consultation), the Basel Committee has, until now, only offered guidance to financial institutions as to how to address climate-related risk, instead of amending the design of the existing prudential framework and recommending that jurisdictions evolve their regulatory frameworks accordingly (**2022 Basel Committee principles on climate risk management**, followed by **FAQs** issued in December 2022). Despite the detail provided in this guidance by the Basel Committee, this principles-based approach generally runs the risk of inconsistent or insufficiently ambitious consideration of climate-related financial risks by financial institutions. In a context marked by intensifying climate impacts, we strongly support the pivot to regulation and a holistic review of the prudential framework as the best course to secure consistent and meaningful treatment of climate risk by financial institutions, thus securing financial system resilience and market integrity.

The changes considered also respond to the need to establish a strong global baseline to prevent fragmentation. Various climate-related disclosure frameworks for private sector institutions, including financial institutions, are being designed or implemented across jurisdictions. The Basel Committee's role is to provide an ambitious global reference point on prudential requirements, including disclosures, and this initiative is welcome to mitigate risks of cross-jurisdictional fragmentation.

By building on the International Sustainability Standards Board's global sustainability disclosure standards (IFRS S1 and S2), the Basel Committee's proposed changes promote interoperability of disclosure regulation across geographies and could support increased readability of climate-related information distilled across sectors and geographies to market participants. The standards designed by the ISSB are being translated into local regulatory requirements at increasing speed across jurisdictions. The ISSB helpfully provides a global baseline for private sector firms generally supporting a building block approach. As this standard is being increasingly taken up, it is helpful for the Basel Committee to evolve its own prudential disclosure framework and to articulate it with that of the ISSB, thereby helping promote consistency and readability of information for market participants.

We firmly believe that the changes proposed by the Basel Committee are also in line with the goals sought by Pillar 3 of the global prudential framework. The goal of Pillar 3 is to enable market participants to evaluate the capital adequacy of banks in front of risks and thus enable market discipline. Considering the forward-looking nature of climate-related risks, and the degree to which these could prove material at a microprudential (and macroprudential) level, this necessarily implies an evolution of the scope of Pillar 3 disclosures to incorporate forward-looking climate-related information, as foreseen in this consultative document.

We generally urge the Basel Committee to mandate the changes proposed in this consultation for all internationally active banks without national discretion.

We also urge the Basel Committee to finalise this work as soon as possible, targeting an implementation date starting January 2025, at least for the qualitative information envisaged in the consultation.

Lastly, while the considered adjustments to Pillar 3 are both welcome and necessary, they are not sufficient to fully address gaps in the global prudential framework regarding climate risk. More work is needed to ensure the global prudential framework is fit-for-purpose in the age of the climate challenge. We urge the Committee to complete the work on reviewing Pillar 1 and 2 of the Basel framework, and propose adequate changes to remediate outstanding gaps, in line with the Q4 2024 communicated timeline.

E3G response to key consultation questions

Qualitative disclosure requirements (questions 11-16)

We fully support enhanced disclosure of qualitative information in relation to climate-related financial risk. Adequate qualitative information is highly relevant to help market participants assess bank readiness in managing climate risks, and is critical information to help contextualise certain metrics and ensure they are decision-useful. We believe, however, that more clarity and specificity is required in this section:

- Qualitative disclosures should generally seek close and detailed alignment with the requirements of the Committee's Principles for the effective management and supervision of climate-related financial risks.
- **We strongly support the Basel Committee's proposal to include transition plan disclosures (Q15/Strategy), but recommend clarifying that plan disclosure should be mandatory for internationally active banks. Transition plan disclosures from financial institutions are critical in properly assessing banks' overall capital adequacy; they are all the more critical in supporting market discipline given that there may be Pillar 1 gaps vis-à-vis climate risk that the Basel Committee has not yet addressed.**

- **In this regard:**
    - The Basel Committee should strive to ensure consistency and comparability of the disclosed transition plan information – by providing specific guidance on the information to be disclosed (e.g. objectives and priorities in terms of emissions reductions, other metrics and targets underpinning emissions reductions objectives, implementation and engagement strategies, etc.), as well as on scenario analysis and key assumptions, as a critical underpinning to this exercise.
    - Transition plan disclosure requirements should take into account and seek alignment wherever possible with work done on this topic by the NGFS and FSB, more advanced frameworks on transition plans such as the UK TPT's Disclosure Framework, the European ESRS, as well as ongoing work by the Singapore MAS on transition planning for financial institutions and the EU EBA on "prudential transition plans".
    - Critically, in determining transition plan disclosure requirements, the Basel Committee should reflect on the fact that this tool is not just about climate risk management but should also constitute the "new normal" for a bank's strategic planning and decision-making. Transition plans disclosure requirements are critical to enable market participants to assess banks' readiness and resilience in a rapidly changing macroeconomic and climate context, with risks materialising at far greater speed than climate scientists had initially foreseen. Assessing this readiness means understanding the degree to which a bank incorporates this new reality in its strategy, and adjusts its internal processes accordingly, including risk management, and governance.
    - Transition plan disclosures should include Scope 3-related emissions and associated targets as mandatory, given that Scope 3 emissions form the largest part of emissions associated with the financial sector.
    - Transition plan disclosures should notably cover progress achieved towards the stated targets/forecasts as well as risk mitigating actions by banks focused on client engagement, escalation/disengagement polices, and transition-linked products.

Quantitative disclosure requirements

- **Questions 17-29:**
    - Mandatory disclosures of Scope 3 emissions in particular as indicators of climate-related financial risks are welcome. The Basel Committee should further work with supervisors to establish a uniform understanding, definitions, and methodologies for climate-related financial risk metrics.
    - Emission disclosures should be viewed in the context of qualitative information such as banks' actions to achieve reductions in the financed GHG emissions (such as engagement with their clients, conditions attached to the provision of financing), in particular in the context of transition planning and transition plan disclosures.
    - Transparency over the underlying emission calculations methodologies, as well as key underpinning assumptions, should be required. The Committee should also provide guidance on which methodologies should be used to calculate the financed emissions to help the banks navigate the uncertainties in this developing field and ensure credibility and comparability of the information.
    - Disclosure of facilitated emissions should be made mandatory and not subject to jurisdictional discretion. With their capital market activities, banks contribute significantly to the financing of fossil fuel and other industries, which are major emitters of GHG and, via this, contribute to the physical and transition risks in the system.

- **Questions 37-41, 49-51:**
    - Disclosure of forward-looking metrics and targets should be mandatory for all jurisdictions, as this information is key when looking at climate-related risks which are by nature forward-looking (as stated in the consultation document itself).
    - However, this may be challenging for certain jurisdictions, in the absence for example of relevant regional transition pathways, including sectoral ones, to support the disclosure of meaningful targets.
    - We encourage Basel Committee members to engage in regular dialogue with relevant counterparts on this matter (e.g. the ISSB, who is closely looking at this issue, central banks from key regions concerned with this matter, regional networks).

- This issue also stresses the importance of disclosing adequate qualitative information (especially through transition plans), to help market participants assess the situation on a case-by-case basis.