Comments and Requests for Clarification
General comments
• **Support** the ongoing efforts of regulators to ensure proper identification, understanding, management, and supervision of risk stemming from climate-related factors. • **Support** integrating climate-related financial risks into existing risk management frameworks and structures. Regulatory supervisors should ensure that climate risks are considered, identified, understood, and managed by financial institutions. • It is the **responsibility of regulators in each jurisdiction to ensure financial institutions manage climate risk in line with the country's just transition objectives, regulatory proportionality, entity's business strategy, and risk appetite**. • The **principles-based approach is appropriate and aligned with the South African regulatory framework approach**. Climate risk is an emerging and rapidly evolving risk discipline. Support the flexibility for supervisors to adopt the principles in a manner that is proportional and suitable for a just transition in their jurisdiction. The country's legal and regulatory frameworks must be aligned with its national climate objectives and climate targets. • **Recommend** that the paper note that banks cannot be the primary enforcers of climate policy, neither should the prudential framework be used as a substitute for direct mechanisms such as taxes or industrial measures. The role of supervisors should be to ensure that risks that can be stemming from climate change are considered by the institutions, identified, understood, and managed. • The challenge for most financial institutions is that most have not focused on what should be done, but on how it should be done. **More benefit would be gained from future standards** for example on how portfolios should be segmented for climate risk reporting (i.e., climate risk reporting classes vs Basel reporting asset classes) to create uniformity in the process. • **Recommend** explicitly state what is not included in the scope of this paper, in particular the position around using stress and scenario testing outputs to determine capital reserve requirements. • **Recommend** being more explicit about what value smaller banks could get. In Section 6: "However, smaller banks and authorities in all jurisdictions can benefit from a structured consideration of the potential impact of climate-related financial risks". The reference to "structured consideration…. of…risks" does not reference the (intended) benefits that smaller banks would gain from applying scenario testing principles set out in this document. • **Recommend** considering regulatory harmonisation at a global level when finalising the principles. Several regulatory authorities around the globe have issued supervisory expectations for climate-related risk management. Global harmonisation is important for standardising reporting and disclosures requirements and to avoid costly duplications and end-user confusion.

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I. Introduction (p. 5 – 6)
The climate risk appetite is also informed by national and sovereign commitments and targets limiting climate warming and protecting biodiversity. Para 8: "Banks should manage climate-related financial risks in a manner that is proportionate to the nature, scale, and complexity of their activities and the overall level of risk that each bank is willing to accept". The use of the verb 'willing' suggests that appetite for climate-related risk is informed only by a firm's strategy, available capital, and other internal measures that are independent of external factors (such as a net-zero commitment for example). **Recommend** enhancing the wording to "…. overall level of risk determined by each bank's strategy as well as firm-specific and national commitments to adjusting portfolios to meeting targets set for lower emissions pathways."
II. Principles for the management of climate-related financial risks (p. 6 - 11)
Corporate Governance (p. 6 – 7)
Principle 1: Banks should develop and implement a sound process for understanding and assessing the potential impact of climate-related risk drivers on their businesses and on the environments in which they operate. Banks should consider material climate-related financial risks that could manifest over various time horizons and incorporate these risks into their overall business strategies and risk management frameworks. [Reference principles: BCP 14, SRP 30, Corporate governance principles for banks]
Recommend that the principles articulate the roles and responsibilities between the board, senior management, and the 3 Lines of Defence.
Principle 2: The board and senior management should clearly assign climate-related responsibilities to members and committees and exercise effective oversight of climate-related financial risks. The board and senior management should identify responsibilities for climate-related risk management throughout the organisational structure. [Reference principles: BCP 14, SRP 30, Corporate governance principles for banks]

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Recommend that the principles articulate the roles and responsibilities between the board, senior management, and the 3 Lines of Defence.
Principle 3: Banks should adopt appropriate policies, procedures and controls to be implemented across the entire organisation to ensure effective management of climate-related financial risks. [Reference principles: BCP 14, SRP 30, Corporate governance principles for banks]
Recommend implementation based on time and proportionality considering the large-scale investments and skills development requirements.
Internal control framework (p. 7 – 8)
Principle 4: Banks should incorporate climate-related financial risks into their internal control frameworks across the three lines of defence to ensure sound, comprehensive and effective identification, measurement and mitigation of material climate-related financial risks. [Reference principles: BCP 26, SRP 20, SRP 30]
Para 19: "The second line of defence…independent climate-related risk assessment…" – This is a focus on the individual climate rating process (for a transaction or a counterparty for example), however much of the second line's role is also portfolio risk management. This includes concentration risk analysis (e.g., to sectors with high levels of climate risk) where exposures are aggregated, and correlations are measured to determine overall levels of risk. We could consider therefore including reference to portfolio risk management.
Capital and liquidity adequacy (p. 8)
Principle 5: Banks should identify and quantify climate-related financial risks and incorporate those assessed as material over relevant time horizons into their internal capital and liquidity adequacy assessment processes. [Reference principles: BCP 15, BCP 24, SRP 20, SRP 30]
Risk management process (p. 8 – 9)

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Principle 6: Banks should identify, monitor and manage all climate-related financial risks that could materially impair their financial condition, including their capital resources and liquidity positions. Banks should ensure that their risk appetite and risk management frameworks consider all material climate-related financial risks to which they are exposed and establish a reliable approach to identifying, measuring, monitoring and managing those risks. [Reference principles: BCP 15, SRP 30]
The long-term nature of climate change considers horizons that can extend significantly beyond those considered by institutions – e.g., Net Zero targets by 2050. While these are high-level principles, additional detail that would be beneficial is the **required data granularity** and **the time horizon** for management of climate-related financial risks, as these risks are **not always congruent with time horizons for traditional risk management processes**, nor is the data readily standardised or available. This will affect how **data is translated into climate risk drivers** and the economic risk factors; how the data links climate-adjusted economic risk factors to exposures; and subsequently how this data is translated into financial risk.
Management monitoring and reporting (p. 9)
Principle 7: Risk data aggregation capabilities and internal risk reporting practices should account for climate-related financial risks. Banks should seek to ensure that their internal reporting systems are capable of monitoring material climate-related financial risks and producing timely information to ensure effective board and senior management decision-making. [Reference principles: BCP 15, SRP 30, Principles for effective risk data aggregation and risk reporting]
"…develop qualitative or quantitative metrics…": This implies that banks have the choice of choosing either qualitative or quantitative. **Recommend** that the "or" be changed to read "and." as both are important. "Banks should consider actively engaging clients and counterparties and collecting additional data to develop a better understanding of their transition strategies and risk profiles": There is a potential challenge relating to data privacy, POPIA, GPDR, and others. Recommend guidance or a statement to clarify that this should be done under relevant regulatory data governance frameworks.
Comprehensive management of credit risk (p. 9 – 10)

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Principle 8: Banks should understand the impact of climate-related risk drivers on their credit risk profiles and ensure credit risk management systems and processes consider material climate-related financial risks. [Reference principles: BCP 17, BCP 19, SRP 20, Principles for the management of credit risk]
Para 32: "…on their credit risk profiles…": this reads as if banks need to measure and report on climate-related risk impacts on their credit risk profile (i.e., 'own risk' as measured by the bank's credit rating). Recommend including an assessment of the risk of the bank's customer risk profiles – i.e., 'obligor risk.'
Comprehensive management of market, liquidity, operational and other risks (p. 10 - 11)
Principle 9: Banks should understand the impact of climate-related risk drivers on their market risk positions and ensure that market risk management systems and processes consider material climate-related financial risks. [Reference principles: BCP 22]
Recommend including the distinction between short-term (sometimes intra-day) market price movements in instruments, versus the more longer-term asset price moves (for example in asset management portfolios). This difference is illustrated by BNP Paribas's response to the Bank of England's request for commentary on their 2021 Exploratory Scenario on the Financial Risks from Climate Change, where they state: "*For trading books, the core need is to prepare for instantaneous shock events linked to climate risk. However, an asset manager will need the longer-term view on what is probably a less liquid portfolio, in order to identify the trajectory and probable 2-degree alignment of their investments*". The wording in Principle 9 is aimed at the available-for-sale trading and hedging book which does not require the same level of model development and time and resource application, as is required for the understanding of long-term climate-related risks and their impact on asset portfolios. As was observed by, and can be inferred from BNP Paribas, the impact of potential climate-related losses on the long-term asset portfolio is more closely related to the chronic nature of gradual climate change effects, while the short-term trading portfolio is more sensitive to extreme (acute) climate impacts. Both can be material.
Principle 10: Banks should understand the impact of climate-related risk drivers on their liquidity risk profiles and ensure that liquidity risk management systems and processes consider material climate-related financial risks. [Reference principles: BCP 24, Principles for sound liquidity risk management and supervision]
Principle 10 focuses on processes to manage climate-related risk impacts from 'funding liquidity' being the ability to finance assets continuously, rather than 'transaction liquidity' which references the ease with which assets can be exchanged for cash or other

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assets. The reference to BCP24 aligns with the wording in this Consultative Document and that is appropriate given the stated intention of 'fostering alignment' it is submitted here to be comprehensive. Recommend considering widening the scope to include market liquidity-related stresses that may be transmitted from climate-related events. This is an opportunity to expand on how climate-related risk drivers might be expected to impact all types of liquidity risks over different (and longer) time horizons.
Principle 11: Banks should understand the impact of climate-related risk drivers on their operational risk and ensure that risk management systems and processes consider material climate-related risks. Banks should also understand the impact of climate-related risk drivers on other risks6 and put in place adequate measures to account for these risks were material. This includes climate-related risk drivers that might lead to increasing strategic, reputational, and regulatory compliance risk, as well as liability costs associated with climate-sensitive investments and businesses. [Reference principles: BCP 25, Principles for the sound management of operational risk, Principles for operational resilience, SRP 20, SRP 30]
Scenario Analysis (p. 11)
Principle 12: Where appropriate, banks should make use of scenario analysis, including stress testing, to assess the resilience of their business models and strategies to a range of plausible climate-related pathways and determine the impact of climate-related risk drivers on their overall risk profile. These analyses should consider physical and transition risks as drivers of credit, market, operational and liquidity risks over a range of relevant time horizons. [Reference principles: BCP 15, Stress testing principles]
Scenario analysis looks at the climate-related pathways (such as the NGFS scenarios) while stress testing looks at severe but plausible scenarios oriented to the near-term horizon.
III. Principles for the supervision of climate-related financial risks (p. 12 - 14)
Prudential regulatory and supervisory requirements for banks (p. 12 - 13)

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Principle 13: Supervisors should determine that banks' incorporation of material climate-related financial risks into their business strategies, corporate governance and internal control frameworks is sound and comprehensive. [Reference principles: BCP 9, BCP 14, BCP 26, SRP 20]
Principle 14: Supervisors should determine that banks can adequately identify, monitor and manage all material climate-related financial risks as part of their assessments of banks' risk appetite and risk management frameworks. [Reference principles: BCP 15, SRP 20, SRP 30]
Principle 15: Supervisors should determine that banks comprehensively identify and assess the impact of climate-related risk drivers on their risk profile and ensure that material climate-related financial risks are adequately considered in their management of credit, market, liquidity, operational, and other types of risk. Supervisors should determine that, where appropriate, banks apply climate scenario analysis. [Reference principles: BCP 17–25, Principles for sound liquidity risk management and supervision, Principles for the sound management of operational risk, Principles for operational resilience]
Responsibilities, powers and functions of supervisors (p. 13 - 14)
Principle 16: In conducting supervisory assessments of supervised banks' management of climate-related financial risks, supervisors should utilise an appropriate range of techniques and tools and adopt adequate follow-up measures in case of material misalignment with supervisory expectations. [Reference principles: BCP 8, BCP 9, SRP 10, SRP 20]

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Principle 17: Supervisors should ensure that they have adequate resources and capacity to effectively assess supervised banks' management of climate-related financial risks. [Reference principles: BCP 9]
Principle 18: Supervisors should consider using climate-related risk scenario analysis, including stress testing, to identify relevant risk factors, size portfolio exposures, identify data gaps and inform the adequacy of risk management approaches. Where appropriate, supervisors should consider disclosing the findings of these exercises. [Reference principles: Stress testing principles]
IV. Questions on the proposed principles (p. 14)
Q1. Has the Committee appropriately captured the necessary requirements for the effective management of climate-related financial risks and the related supervision? Are there any aspects that the Committee could consider further or that would benefit from additional guidance from the Committee?
The Principles for the Effective Management of Climate Change emphasises the monitoring and management of a specific risk/threat that can lead to multiple consequential risks. The BCBS can consider applying a more generic approach to the monitoring of such large-scale events as these principles can be applied to any threat/risk. Considerations around business/strategic risk and the associated financial loss may not be sufficiently detailed in the paper. It is only briefly mentioned in paragraph 40. Given the long-time horizon, these risks are likely to have the biggest impact.
Q2. Do you have any comments on the individual principles and supporting commentary? **(Note:** Members may wish to refer to any comments under the respective Principles above)
Recommend Ongoing monitoring and recommendations: The BCBS should continue focusing on driving harmonisation of supervisory practices given the fragmented regulatory landscape to date. We would recommend the BCBS regularly monitor and report on those practices, issue recommendations on the back of those findings to promote international alignment.

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Recommend developing a roadmap: The BCBS supplements the principles with an agreed implementation roadmap to align implementation dates across its member jurisdictions. Although some supervisors have published their guidelines, full implementation of those supervisory expectations will take a couple of years. Prioritisation of those principles and elements of those principles, related key milestones, and endpoint should be agreed upon at the Basel level and then followed in local implementation plans. **Recommend BCBS coordination and clearinghouse role**: The BCBS takes on the coordination and a clearinghouse role in the roll-out of the supervisory exploratory scenarios at the local level. A coordinated approach would be beneficial to supervisors as it would facilitate information exchange, lessons learned thru improved consistency and comparability, and accelerate capacity building. Lesson learned could also be shared with the Network of Central Banks and Supervisors for Greening the Financial System (NGFS) and support refinement and updates of NGFS scenarios. **Recommend proportionality at all levels:** The principles should be applied proportionally at the consolidated and local subsidiary levels, which may differ significantly. This applies to the governance, risk management, and disclosures requirements.
Q3. How could the transmission of environmental risks to banks' risk profiles be taken into account when considering the potential application of these principles to broader environmental risks in the future? Which key aspects should be considered?
There are still many data gaps and uncertainty resulting in a large margin of error. Capturing the impact of environmental risks other than climate risks on other existing risk categories is challenging due to the lack of data, methods, and academic research While scenarios analysis and stress testing will provide good measures of impact to the risk profile, banks must ensure that these include forward-looking scenarios and not be based on historical stresses. Directional results and quantum should be more important than attempting to forecast exact numbers. The development of a uniform definition of ESG risks, including physical risks and transition risks; the latter shall comprise the risks related to the depreciation of assets due to regulatory changes. Challenge of incorporating financial risk driven by environmental risk. Environmental risk unlike Climate risk has no one distinct quantitative driver (Carbon emissions) and hence industry-wide definition on data relating to Environmental risk needs to be considered. Environmental risk is also multi-faceted. Pollution can be across the land, water, air, deforestation, water shortages, etc, and loss of biodiversity will require different data sets. Time horizons for different environmental risks may also differ (Biodiversity loss impact may be longer-term than more acute pollution).

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The development of appropriate qualitative and quantitative criteria for the assessment of the impact of ESG risks on the financial stability of institutions in the short, medium, and long term; such criteria shall include stress testing processes and scenario analyses to assess the impact of ESG risks under scenarios with different severities. **Capital treatment:** We would strongly encourage any future decision to amend the capital treatment based on climate-related financial risks considerations to be agreed at the BCBS level and avoid a unilateral decision by Basel members. This could have unintended consequences, distort capital allocation decisions by international banks, and will raise level playing field consideration.