



# **PROPOSED GUIDANCE FOR NEW YORK STATE- REGULATED BANKING AND MORTGAGE INSTITUTIONS RELATING TO MANAGEMENT OF MATERIAL FINANCIAL RISKS FROM CLIMATE CHANGE**

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# Purpose

Support banking and mortgage institutions (“Regulated Organizations”) in managing the financial risks from climate change (“climate-related financial risks”).



# Approach

- Proportionate and principles-based guidance
- Focus on material risks
- No cut-off by asset size
- Integrate into existing risk management framework
- Implementation timeline to come, informed by comments
- Establish basis for continued supervisory dialogue
- Does not dictate what customers/investments are permitted; does not opine on specific risk assessments
- Fair Lending and CRA—fair access to credit is critical



# Basis for Proposed Guidance

**Alignment with existing U.S. risk management guidance, exam manuals:** FRB, OCC, FDIC

**Leverages climate-related supervisory expectations and guidance:**

- OCC, FDIC and FRB
- Basel Committee on Banking Supervision
- Bank of England
- European Central Bank

**Feedback from U.S. regulators:** FRB, OCC, FDIC, NCUA, FHFA, CFPB

**Industry roundtables:** IIB, NYBA, NYMBA, IBANYS, NYCUA



# Structure of the Proposed Guidance

- I. Introduction
- II. Financial Risks from Climate Change
- III. Overarching Themes
- IV. Supervisory Guidance
- V. DFS Feedback Request: by March 21, 2023



## II. Financial Risks from Climate Change

### Two Primary Channels: Physical and Transition Risks

#### ➤ Physical Risks: Acute and Chronic

- Increasing frequency, severity, and volatility of acute events
- Chronic shifts in weather patterns (sea level rise, heat waves, drought)
- Greater likelihood of extremes

#### Potential economic effects:

- Reduced revenue, lower property values and household wealth, increased costs



## II. Financial Risks from Climate Change (cont.)

### ➤ **Transition Risk:**

- Arises from shifts in policy and regulations, new technologies, changing consumer and investor preferences, and liability risks

### **Potential economic effects:**

- Revaluation of assets, increased capital costs, decreased profitability, property values and household wealth
- Both channels: Direct and indirect impacts on financial institutions



## III. Overarching Themes

- A. Managing Climate-Related Financial Risks While Providing Fair Lending to All Communities
- B. Proportionate Approach





## III.A. Managing Climate-Related Financial Risks While Providing Fair Lending to All Communities

- Manage climate-related financial risks prudently and comply with obligations to ensure fair access to capital and credit
- **Potential unintended consequences:** disproportionate harm to LMI/minority communities must be minimized and affirmatively mitigated
- Climate risk management must not be based on disinvesting or making access to credit more difficult/expensive
- **DFS Industry Letter February 2021:** banks may be eligible for credit under NY's Community Reinvestment Act for supporting community resiliency



## III.B. Proportionate Approach

- Smaller organizations  $\neq$  less climate-related financial risk
  - Can have concentration of risk through less diversification
- Guidance not limited to larger organizations
- Governance, strategy, and risk management approach should be tailored to organization's type and degree of exposure
  - Not one-size-fits-all: organizations have different resource levels, capacity, and complexity
- Group's/FBO Head Office policies, procedures, and processes: need sufficient transparency for U.S. regulators to assess adequacy relative to local expectations



## IV. Supervisory Guidance

- A. Corporate Governance
- B. Internal Control Framework
- C. Risk Management Process
- D. Data Aggregation and Reporting
- E. Scenario Analysis



## IV.A. Corporate Governance

### (i) Business Environment and Strategy

- Develop/implement processes to understand and assess potential impacts of physical and transition risk drivers on business environment and strategy
- Consider impacts over short, medium, and long term
- Align climate risk-mitigation strategies with and support broader strategy, risk appetite, and risk management framework
- Any climate-related commitments should be consistent with internal strategies and risk appetite



## IV.A. Corporate Governance

### (ii) Board and Management Oversight

- Governance framework should ensure risk management processes are sufficient to identify, measure, monitor, and manage climate-related financial risks
- Board role includes integration into risk appetite framework, defining materiality, actively overseeing risk-taking activities, and ensuring related policies and procedures are adequate, taking dynamic approach
- Senior management to execute overall strategic plan, manage material risks, and report to the board regularly on level and nature of these risks
- Adapt existing organizational structures or establish new ones; cross-functional approach



## IV.A. Corporate Governance

### (iii) Policies, Procedures, and Limits

- Embed management of material risks in policies, procedures, and controls across all relevant functions and business units
- Align with strategy and risk appetite set by board
- Policies and procedures should provide guidance for the day-to-day implementation of broad business strategies, including climate-related risks



## IV.B. Internal Control Framework

- Incorporate material climate risks into internal control frameworks across the three lines of defense:
  - **Risk-taking:** assess climate-related financial risks during client onboarding, credit application, and credit review
  - **Risk management:** independent climate-related financial risk assessment and monitoring; compliance reviews
  - **Internal audit:** independent reviews of control framework and systems
- Establish clear lines of authority and responsibility



## IV.C. Risk Management Process

- Address through existing risk management framework and risk types in line with risk appetite
- Apply risk management system to climate-related financial risks:
  - Identify Risk (IV.C.(i) of Proposed Guidance)
  - Measure Risk (IV.C.(ii) of Proposed Guidance)
  - Monitor Risk (IV.C.(iii) of Proposed Guidance)
  - Control Risk (IV.C.(iv) of Proposed Guidance)
- Assess impact of physical and transition risks as drivers of existing risk types





## IV.C. Risk Management Process

### (v) Climate Change's Impact on Existing Risk Factors

- Credit Risk
- Market Risk
- Operational Risk
- Liquidity Risk
- Legal/Compliance Risk
- Strategic Risk



## IV.D. Data Aggregation and Reporting

- Develop risk data aggregation capabilities and internal risk reporting practices to monitor material climate risks
- Timely internal reporting of climate risk data
- Sophistication of systems should be consistent with complexity, scale, and diversity of operations and level of exposure to climate risks
- Consider enhancing data infrastructure and existing IT systems as needed



## IV.E. Scenario Analysis

- Utility as a Forward-Looking Risk Management Tool
- Objectives can include:
  - Assessing the resilience of business models and strategies to a range of climate scenarios
  - Identifying and measuring vulnerability to relevant climate-related risk factors, including physical and transition risks
  - Estimating exposures and potential losses
  - Determining materiality of climate-related financial risks, and
  - Identifying data gaps and assess adequacy of existing processes
- Climate scenario analysis  $\neq$  traditional stress testing
- Use a proportionate approach to build sufficient capacity and expertise



## V. Feedback Request: Specific Questions

- 1. Should a timeline for implementation be established?**
  - If yes, what timeline and what is the reasoning supporting that timeline?
- 2. How can smaller institutions benefit from climate scenario analysis?**
  - What does appropriate climate scenario analysis look like for them?
  - Which kind of support do they need in establishing these scenarios?
- 3. Should existing regulatory reporting requirements be supplemented to cover exposure to material financial risks from climate change and their management of such risks?**
  - If so, what should the supplemental report look like?



## V. Feedback Request: Specific Questions (cont.)

### 4. Other Considerations:

- Are there other aspects of climate-related financial risks that the Guidance should consider?
- Are there other aspects of the Guidance that would benefit from further clarification, context, or reframing?



## V. Feedback Process

- **DFS Webpage:**  
[https://www.dfs.ny.gov/industry\\_guidance/climate\\_change](https://www.dfs.ny.gov/industry_guidance/climate_change)
- **Submit feedback to:** [banking\\_climate\\_guidance@dfs.ny.gov](mailto:banking_climate_guidance@dfs.ny.gov)
- **Deadline:** 11:59 p.m. EDT on March 21, 2023
- **Who can provide feedback?** – Anyone and everyone
- **All submissions will be posted**, including names and affiliations of those providing feedback
- **Feedback template:** available on webpage



# V. Feedback Template

Template for Feedback																				
Proposed Guidance for New York State Regulated Banking and Mortgage Organizations Relating to Management of Material Financial Risks from Climate Change																				
Deadline: March 21, 2023 at 11:59 pm EST																				
Affiliation																				
Name										Title										
Email address										Phone number										
<p>Please enter your feedback on this chart. Part A is for responses to the four Questions for Public Feedback on page 12 of the Guidance. Part B is for feedback on the contents of the proposed Guidance. When entering feedback in Part B, please make sure that:</p> <ul style="list-style-type: none"> <li>- each entry deals with a single issue only;</li> <li>- you indicate the relevant section by using the drop down menu in the Section column;</li> <li>- you indicate the relevant paragraph(s) by specifying the paragraph number(s) in the Paragraph Number(s) column; and</li> <li>- you indicate whether your suggestion is a proposed amendment, clarification or deletion.</li> </ul> <p>Please feel free to insert more rows if you have more entries.</p> <p>If you have general feedback not tied to a specific section, please enter it in Part C below.</p> <p>All submissions, including the names and affiliations of the submitters, will be posted on DFS's website.</p> <p>Please submit your feedback to <a href="mailto:banking_climate_guidance@dfs.ny.gov">banking_climate_guidance@dfs.ny.gov</a></p>																				



# V. Feedback Template (cont.)

A. Feedback on the Questions for Public Feedback				
#	Question	Question Number	Type of Feedback	Detailed Feedback
1	Timeline for implementation	V.1	Feedback	
2	Climate scenario analysis	V.2	Feedback	
3	Disclosure	V.3	Feedback	
4	Other aspects to consider	V.4	Feedback	





## V. Feedback Template (cont.)

### B. Feedback on the Proposed Guidance

#	Section	Paragraph Number(s)	Type of Feedback	Detailed Feedback
1				
2				
3				

### C. General Feedback

#	Section	Paragraph Number(s)	Type of Feedback	Detailed Feedback
1	General feedback	N/A	Feedback	



Contact:

[Banking\\_Climate\\_Guidance@dfs.ny.gov](mailto:Banking_Climate_Guidance@dfs.ny.gov)

