Template for comments

Guide on the management and disclosure of climate-related and environmental risks

Institution/Company
d-fine GmbH

Contact person

Mr/Ms

First name

Surname

Email address

Telephone number

General comments

Template for comments

Guide on the management and disclosure of climate-related and environmental risks

Please enter all your feedback in this list.
When entering feedback, please make sure that:
- each comment deals with a single issue only;
- you indicate the relevant article/chapter/paragraph, where appropriate;
- you indicate whether your comment is a proposed amendment, clarification or deletion.

Deadline: 25 September 2020

ID	Chapter	Paragraph	Expectation or box number	Page	Type of comment	Detailed comment	Concise statement as to why your comment should be taken on board	Name of commenter	Personal data
1	Chapter 6	6.1	Expectation 7.5	31	Clarification	Expectation 7.5 states "Where climate-related ... risks are deemed to have an impact from an economic perspective, institutions are expected to consider in the normative perspective the potential impact on regulatory capital ratios going forward..." Since the impact of climate risks may occur on much longer time scales, and typically well beyond the horizon of the normative perspective, even if an economic impact is anticipated, it typically is not possible to measure a material effect in the normative perspective, of course depending on the specific nature of the adverse scenario. Therefore, it would be very important for the practical implementation of the ECB guide to clearly state how a financial institition should proceed in case economic and normative perspective are diverging in terms of impact of climate and environmental risk. In particular, pillar 1 parameters, which might be used as a basis for the normative perspective and its REA calcualtion as well, might not contain any climate impact due to their backward-looking nature (derived from historical data) and a short forward-looking horizon (1 year).	The inclusion of climate risks, which span a much larger time horizon than usual in risk management, should not lead to inconsistencies with previous regulations and guidelines, e.g. in terms of validation, back-testing and consistency requirements for pillar 1 and 2 risk models, as climate effects might be not yet significant in a statistical sense.	,	Publish
2	Chapter 6	6.2	Expectation 8.1	32	Clarification	In case climate risks are already measurable and material, they would be picked in the risk inventory, risk measurement, as well as in the credit-grating process and credit processing. However, it might turn out that - due to long time horizon at least of physical climate risks - that as of now no material impact on the borrower's default risk can be observed. A clarification is needed, how an institution should proceed in this case.	The exact measurement of the impact of climate and enviromental risks, on top of the established credit risk factors, is a challenge, and not every institution will be able to perform that measurement as of now. Therefore there should be a guidance on how to meet ECB's expectations.	,	Publish
3	Chapter 6	6.2	Expectation 8.2	32	Clarification	Credit risk ratings are derived from and depend on historical observations of defaults and losses. As outlined in the EBA guideline on PD and LGD estimation, there are clear rules on how to calibrate and validate such ratings. Introducing a qualitative adjustment for climate risk that is not yet visible in historic observations, might violate validation requirements and lead to a non-compliance with IRB requirements which specifically focus on a derivation from internal data. In case the expectation 8.2 has to be implemented in practice, a clear guidance is needed on how the validation requirements are to be met, or, how the "climate overlay" should be reconciled with existing requirements during IRB model development and validation. Additionally, the ECB guide should clearly state which expectations are applicable for pillar 2 / ICAAP risk assessment and which are expected under pillar 1 / IRB approach.	Under pillar 2, there is considerable more methodological freedom compared to the strictly regulated pillar 1 methods. Therefore it is crucial for implementation of the ECB guide to clearly understand the ECB's expectations under pillar 1 and 2, and their consistency with previous guidelines e.g. EBA/GL/2017/16.	,	Publish

4	Chapter 4	4.1	Expectation 1.1	15	Amendment	The formulation of the expectation only addresses physical risks ("climate change and environmental degradation"); transitional risks are not directly included in the expectation, however also stated in the description of the expectation on the following page.	The first "bold" sentence of each expectations should be interpretable as the heading of the expectation, i.e. should be complete and fully reflect the following detailed description of each expectation.	,	Publish
5	Chapter 4	4.2	Expectation 2.1	17&18	Clarification	As stated in the explanation of the expectation, longer-term (>5 years) effects should also be considered via scenario analyses. However, scenarios analyses usually and for valid reasons focusses on the (stress) impact over the next (eg 3-5) years, hence the longer-term effects will most likely have no impact within the scenario analysis horizon, i.e. will not be material. It should be clarified in more detail how longer-term effects should be analysed in scenario analyses.Potential methods are described e.g. in https://www.d-fine.com/en/news/detail-default/climate-risks-icaap-stress-tests/	Due to the methodological difficulties in measuring (stress) impact over a very long time horizon, more guidance and expectations should be given on how long-term effects due to climate-related and environmental risks should be captured within the shorter time horizons considered in bank and risk management.	,	Publish
6	Chapter 4	4.2	Expectation 2.1	17&18	Amendment	The expectation should mention further potential methodologies or tools (next to scenario analyses) on how the materiality assessment of climate-related and environmental risks could be performed.	Mentioning and refering only to one methodology in the expectation fosters the impression that the ECB expects all banks to definitely use this methodology and leaves no freedom for other methodologies.	,	Publish
7	Chapter 5	5.1	Expectation 3.2	20	Clarification	The term "all policies" (last sentence of first paragraph of Expectation 3.2) is too general, hence should be stated in more detail; the text should be altered such that it should be reviewed whether climate and environmental risks are sufficiently captured in policies.	The formulation of the expectation should be more precise.	,	Publish
8	Chapter 4	4.1	Expectation 1.1	15	Clarification	It is undisputed that climate-related changes may lead to higher unemployments or economical crisis. However, this is not necessarily so. Shouldn't general economic shocks, unless explicitely and inseperately linked to the climate-related scenario, be treated in general stress test scenarios?	We believe, in order to provide appropriate strategic control impulses, scenario and sensitivity analysis related to climate and environmental changes should not have a significant overlap with (already implemented) general economic views. From expectation 1.1 it is not clear whether that view is shared.	,	Publish
9	Chapter 4	4.2	Expectation 2.1	18	Amendment	Long-term effects need to be included in an appropriate risk-assessment. However, long term forecast of the balance sheet figures over time horizons longer than 5 years are generally error-prone, if not impossible. We suggest that, under certain circumstances, it should also be allowed to bring forward future risks to a shorter time horizon on a what-if basis. The current formulation seems to be very prescriptive. Details on a potential alternative approaches can be found here: https://www.d-fine.com/fileadmin/user_upload/d-fine_Climate_Risk_in_ICAAP_and_Stresstests_EN.pdf	Long term-forecasts on time-horizons usually require strong assumptions on the portfolio and balance sheet (e.g. a static balance sheet assumption) which is related to high estimation errors. It should be left open to banks to apply other approaches to include long-term effects in their scenario analysis where appropriate.	,	Publish
10	Chapter 5	5.4	Expectation 6.2	26	Clarification	The Guidelines will be applicable by its day of application. However, adopting the IT systems and collecting and processing all relevant data for the measurement and reporting of climate-related and environmental risks is a significant workload, hence it is hardly feasible to implement it on the short term. The expectation should be clarified with this respect and mention longer transitional periods.	Expectations on implementation timelines and transitional periods should be stated in the Guide.	,	Publish
11	Chapter 5	5.4	Expectation 6.4	27	Clarification	The Guidelines will be applicable by its day of application. However, adopting the IT systems and collecting and processing all relevant data for the measurement and reporting of climate-related and environmental risks is a significant workload, hence it is hardly feasible to implement it on the short term. The expectation should be clarified with this respect and mention longer transitional periods.	Expectations on implementation timelines and transitional periods should be stated in the Guide.	,	Publish
12	Chapter 6	6.1	Expectation 7.2	29	Clarification	As stated in previous expectations (e.g. 7.1), climate-related and environmental risks are not to be seen as individual risk categories but rather risks drivers for already existing risk categories such as credit risk. As such, climate-related and environmental risks should be considered within the quantification of the established risk categories (see e.g. section 6.2). Hence, the formulation of the expectation should be adjusted to "capture" or "considered within risk quantification".	Expectations given within this Guide should be consistent to each other.	,	Publish

13	Chapter 6	6.1	Expectation 7.5	31	Clarification	The sentence "In the same vein, the ECB expects institutions to incorporate climate change, in particular the energy transition, into the assessment from an economic value perspective" is too specific as it explicitey states some types of risks and events which should be captured in the risk quantification within the economic perspective, independent of result of the materiality assessment of these risks / events.	Expectations on risk measurement should always explicitey take into account whether sub-types of climate-related and environmental risks are material for an institution of not.	,	Publish
14	Chapter 6	6.2	Expectation 8.2	32	Clarification	It should be clarified that new risk indicators / ratings / risk classification procedures can additionally be introduced (as stated in the examples given in Box 8), in contrast to only allowing to "adjust" existing risk classification procedures. This is especially important regarding existing IRB rating models as the adjustment of these models would trigger the model change process and would have implications on all IRB requirements such as validation and back-testing (which as such is most likely not feasible due to the lack of historical data).	There should be stated a clear expectation of weather the expectations reflects only models used within pillar 2 or if the expectation also impacts pillar 1.	,	Publish
15	Chapter 5	5.2	Expectation 4.2	22	Clarification	The meaning of the sentence "It is also expected that risk appetite arrangements and boundaries are decided before commercial targets" is unclear.	Considering climate-related and environmental risk within the risk appetite statement and processes is very important. The formulation of the expection, however, is unclear about how it can be	,	Publish
16	Chapter 6	6.5	Expectation 11	38	Clarification	Climate-related and environmental risks mostly materialise in the medium to long term, i.e. after the planning horizon of 3-5 years. Expanding the planning horizon to more than 5 years or even to some decades is not feasible. It should be clarified how medium to long term effects should be reflected within the planning time horizon of 3-5 years. See as well: https://www.d-fine.com/en/news/detail-default/climate-risks-icaap-stress-tests/	Due to the methodological difficulties in measuring (stress) impact over a very long time horizon, more guidance and expectations should be given on how long-term effects due to climate-related and environmental risks should be captured within the shorter time horizons considered in bank and risk management. Additionally, consistency of the expectations with other regulations (e.g. ECB Guide on ICAAP) is crucial	,	Publish
17	Chapter 6	6.5	Expectation 11	38	Clarification	It should be clarified how longer term effects should be reflected in stress testing in the economic perspective, in particular since stress testing in the economic perspective is mostly no multi-year projection (see footnote 46 in the ECB Guide on ICAAP). Please refer to https://www.d-fine.com/en/news/detail-default/climate-risks-icaap-stress-tests/ as well.	Due to the methodological difficulties in measuring (stress) impact over a very long time horizon, more guidance and expectations should be given on how long-term effects due to climate-related and environmental risks should be captured within the shorter time horizons considered in bank and risk management. Additionally, consistency of the expectations with other regulations (e.g. ECB Guide on ICAAP) is crucial	,	Publish
18	Chapter 6	6.5	Expectation 11	37	Amendment	In expectation 11 it is mentioned that "for physical risk, institutions are expected to consider using scenarios that are in line with scientific climate change pathways, such as IPCC or IEA scenarios". This also applies to transition risks, since especially the IEA scenarios tend to follow the approach to articulate different policy outcomes (i.e. level of temperature increase) and the energy and economic pathways that would result, with some probability, in achieving temperature increases around the desired outcome, i. e transition scenarios. Therefore "for physical risks" should be deleted in the sentence.	The IEA scenarios are examples of transition scenarios to a low carbon economy while the IPCC scenarios based on Representative Concentration Pathways are examples of physical climate change scenarios.	,	Publish
19	Chapter 6	6.5	Expectation 11	37	Clarification	Institutions should consider different scenarios when conducting scenario analysis and stress testing with respect to climate-related and environmental risks. However no guidance is given here which range of different scenarios the institution should consider, e. g. disorderly transition scenario, paris-aligned transition scenario, hot house world scenario. Referencing other guidelines here, as for example the guide to climate scenario analysis by the NGFS, could be helpful to provide institutions an overview of the possible range of transition and physical risk scenarios (scenarios framework) and a starting point for selecting relevant scenarios for their analysis.	As stated in the NGFS guide to climate scenario analysis "there is an abundance of climate models to choose from, and it is not immediately clear which ones are most relevant. In addition, the field of climate modelling is technical and difficult to penetrate for non-experts." The NGFS Reference Scenarios mentioned in the guide to climate scenario analysis or other guidance by the ECB could be helpful here.	,	Publish

20	Chapter 7	7	Expectation 13.4	43	Clarification	Expectation 13 states that "institutions are expected to publish meaningful information ..., as a minimum, in line with the European Commission's Guidelines on non-financial reporting: Supplement on reporting climate-related information". In the European Commission's Guidelines on non-financial reporting: Supplement on reporting climate-related information on page 8 in chapter Materiality it is mentioned that "...references to risks should be understood to refer both to risks of negative impacts on the company and to risks of negative impacts on the climate", i. e. a double materiality perspective, also known as inside-out and outside-in perspectives (refer to Non-Financial Reporting Directive). However, Expectation 13.4 explicitly mentiones the financial materiality only. Please clarify why a restriction to only one of the two perspectives was taken here.	Including also the environmental perspective would improve consistency to other guidelines and regulations, e. g. the European Commission's Guidelines on non-financial reporting: Supplement on reporting climate-related information and the Non-Financial Reporting Directive.	,	Publish
21	Chapter 7	7	Expectation 13.5	43	Clarification	Expectation 13 states that "institutions are expected to publish meaningful information ..., as a minimum, in line with the European Commission's Guidelines on non-financial reporting: Supplement on reporting climate-related information". However, Expectation 13.5, which specifies the content of climate-related and environmental risk disclosure, only lists a subset of the key performance indicators specified in the European Commission's Guidelines on non-financial reporting: Supplement on reporting climate-related information in Annex I, 5. KPIs, page 31-33. Please clarify why the other KPIs, as for example the volume of financial assets funding sustainable economic activities contributing substantially to climate mitigation and/or adaptation according to the EU taxonomy, are not included in the minimum disclosure expectations specified with expectation 13.5.	Not mentioning some of the KPIs included in the European Commission's Guidelines on non-financial reporting: Supplement on reporting climate-related information might lead to confusion on the institutions side which KPIs to disclose. Including them explicitly in expectation 13.5 would improve consistency to the EC Guidelines.	,	Publish
22	Chapter 6	6.3	Expectation 9	34	Clarification	This section refers to climate-related events with an impact to operational risk, reputational risk an liability risk. As especially reputational risk is explicitly excluded in operational risk, the relevance of this section for non-financial risk might become clearer if the section would be renamed to "Operational risk and non-financial risk management".	Institutions might find reputational risk to be non-material, contrary to operational risk. Therefore, operational risk and other non-financial risks (including reputational risks) might need to be treated differently. This requires a clarification whether the impact of cimate-related events should be assessed in the operational risk framework or in a general risk assessment that includes non-financial risks.	,	Publish
23	Chapter 6	6.4	Expectation 10	36	Clarification	The draft guidelines reference the importance of environmental and climate-related risks for banking book positions. However, the formulation of the paragraph quoted in the following is unclear as to which positions shall be recognized in general. While the draft guidelines reference the credit spread risk of banking book positions, they as well mention the total equity exposure. "With specific reference to the credit spread risk component of banking book positions, institutions are expected to assess the relevance of the credit spread among all the drivers of overall market risk. This is relevant when considering, among others, that financial instruments issued by companies belonging to sectors perceived as environmentally unsustainable and which do not adopt a comprehensive sustainable management approach might suffer an abrupt decline in their value. In the same vein, the value of equity exposures should be monitored on an ongoing basis to assess whether their value has been negatively affected by a change in the perception of the issuer's riskiness, specifically owing to climate-related and environmental risks."	Since environmental and climate-related risk are typically long term, especially banking book positions can be affected on the relevant time scale and might be considered relevant.	,	Publish

24	Chapter 6	6.4	Expectation 10	37	Clarification	The draft guideline stresses the importance of stress testing for market risk management. An integral part of the stress testing guidelines (e.g. EBA/GL/2018/04) is sensitivity analysis. In particular for environmental and climate-related risk sensitivity analysis can be very usefull. We therefore suggest to reference also to sensitivity analysis as an adequate alternative to stress testing. Please refer to https://www.d-fine.com/en/news/detail-default/climate-risks-icaap-stress-tests/ as well.	Independent of a specific scenarios, sensitivitites and changes of sensitivities in the course of time may act as usefull indicators for risk and changing risk positions.	,	Publish
25	Chapter 6	6.5	Expectation 11	38	Clarification	The draft guidelines reference the forward-looking horizon of at least three years in the ICAAP as well as the longer time horizons for climate-related und environmental risks and that institutions are expected to take developments beyond this minimum horizon into account. Important for the ICAAP, however, are intrinsically consistent scenarios. In the normative perspective as well as in the economic perspective. How should this consistency be established taking into account the different time scales of developments?	Consistent scenarios for the ICAAP are important to obtain sound results as well to derive meaningful risk management actions.	,	Publish
26	Chapter 6	6.1	Expectation 7.2	29	Clarification	Institutions are expected to adequately quantify the climate-related and environmental risks. However, sound and robust methodologies are not available yet and the development and market standards will still take some time. Currently it is not obvious whether sound and robust quantitative metrices can be developed in the course of time. The text should clarify whether qualitative statements are accepted as general alternative, or at least for a transitional period.	For physical but especially for transition risk quantitative methods may be impossible to develop due to lack of historical or comparable data to calibrate models. Whereas expert judgment can be a reasonable and recognized alternative, in particular when it involves the long-term, more strategical time horizon.	,	Publish
27	Chapter 5	5.4	Expectation 6.2	27	Amendment	The draft guidelines mentions that instutions may not meet the expectation due to the current lack of common definitions, taxonomies and data gaps. The guidelines should clarify a possible schedule up to when or whether institutions will be provided with common definitions and taxonomies.	Common taxonomies and definitions could be provided, for example, by competent authoriries fostering comparability accross institutions.	,	Publish
28	Chapter 5	5.2	Expectation 4.2	22	Clarification	The draft guidelines expect institutions to assign quantitative metrics to climate-related and environmental risks, acknowledges, however, the current lack of common definitions and taxonomies are still under development and admit qualitative statements as intermediate steps. Currently it is not obvious whether sound and robust quantitative metrices can be developed in the course of time. The text should clarify whether qualitative statements are accepted as general alternative.	For physical but especially for transition risk quantitative methods may be impossible to develop due to lack of historical or comparable data to calibrate models. Whereas expert judgment can be a reasonable and recognized alternative.	,	Publish
29	Chapter 6	6	Expectation 6	28	Clarification	Expectation 6 states "Building on the previous chapter, this section provides detailed guidance on integrating climate-related and environmental risks into credit, operational, market and liquidity risk management, as well as into the ICAAP, including risk quantification by means of scenario analysis and stress testing". Within this preface, ICAAP is mentioned explicitly. We recommend to include a reference to ILAAP as well.	ICAAP and ILAAP are to equivalent control frameworks for comprehensive bank steering. ECB's ICAAP and ILAAP guidelines - a result from the joint multi year plan - are symmetrical and both frameworks form a distinct part of SREP evaluation. Liquidity management is a central part of the ILAAP and covered within the preface of chapter 6. However, the scope of ILAAP is more general covering for example risk quantification, scenario analysis and stress testing from	,	Publish
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