EUROPEAN CENTRAL BANK

BANKING SUPERVISION

Template for comments

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

Institution/Company

Deutsche Bank

Contact person

Mr/Ms

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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 1		1	3	Clarification	From the webinar and public hearing, we understand that the ECB intends to treat this Guide as a roadmap, with banks advancing on the given path throughout the next years; not expecting immediate full compliance. We agree with such an iterative approach, which would be in step with other international regulators such as the Bank of England or the Hong Kong Monetary Authority. We propose a staggered approach for the ECB Guide: Discussions with supervised banks can start in 2021, and banks can give regular updates on their progress. In June 2022, there can be a stock-take on how far institutions have been able to advance in the implementation of the supervisory expectations. This is to ensure consistency of the supervisory dialogue with regulatory timetables. EBA has not yet completed its mandate included in CRR2 to integrate ESG factors into SREP (to go live in June 2022) and reflect on the prudential treatment of sustainable finance assets. The EBA Guidelines on loan origination and monitoring referenced in the ECB Guide were finalised in May 2020, still need to be transposed by national competent authorities and will be applicable by 30/06/2021 with a transitional arrangement of up to 3 years. As both pieces are interdependent with some requirements in the ECB Guide (see below for more details), timelines should be closely aligned. The staggered approach should also take account of (i) the nature of environmental risks (by order of importance, e.g. climate, water scarcity), clarifying which systemic environmental risks will be covered (vs idiosyncratic risks); (ii) the risk type (by order of importance, e.g. credit & operational risk, market and liquidity risk); and (iii) the scope of clients (by order of importance, e.g. large corporates / SMEs / financial institutions).	There are challenges such as the unavailability of certain required data or the fact that there is an emerging rulebook for climate-related disclosure but not yet for wider environmental factors.We encourage the ECB to continue its laudable approach of international alignment of processes. The UK PRA has instituted industry-led working groups on the process of detailing environmental and climate-related risk frameworks. We propose a similar cooperation with the banking industry to ensure reasonable timelines in the integration.	,	Don't publish

2	Chapter 2	2.2		6	Clarification	In line with our response on section 1, institutions will be able to compare their current practices to the ECB standards in early 2021 and develop a roadmap towards compliance. This approach takes account of significant gaps re climate related client data (e.g. Scope 3 emissions), and a lack of common understanding of what metrics to be used. As explained above, there should be a phase-in period, working towards compliance with the expected regulatory requirements by the EBA (mandatory ESG disclosure in pillar 3) by June 2022.	See above	,	Don't publish
3	Chapter 3	3.1		10	Clarification	the ECB needs to clarify the meaning of “environmental risks”, e.g. referring to environmental degradation that has systemic characteristics, such as land usage or water shortages. The work of the Technical Expert Group on the EU Taxonomy and the ESAs’ draft RTS on ESG disclosures (Annex I) contain some definitions and references to environmental factors and degradation, especially as part of the “do no significant harm” assessments. These could serve as a first, general point of reference for environmental factors –they focus on positive sustainability contribution and are not suitable for detailed risk assessment. In any case, the ECB should exclude environmental hazard that may have idiosyncratic characteristics, may be hardly predictable, and may not be reflected in strategic and business planning. We suggest to use the term “environmental risk drivers” to avoid confusion with internal risks within the risk management framework. External impacts from these drivers would then link to internal risk management framework categories.	There is no official definition of the terms “environmental risks / degradation” yet. Climate risks are commonly described as physical and transition risks. In contrast, environmental hazard typically has idiosyncratic rather than systemic characteristics.	,	Don't publish
4	Chapter 4	4.2	2.2	18	Amendment	As described above (in the first comment), the level of application of metrics and KPI should follow a staggered approach. This approach should recognise that full integration into business and risk strategies remains dependent on further progress in the development of climate and environmental risk frameworks.The wording should also be changed to “business and risk strategies”.	This particular expectation introduces new factors to be considered in the business planning process in financial institutions. It also goes beyond the content of the TCFD recommendations, which means that banks will need time to implement this. The wording change is appropriate as likely risk appetite will be in the risk strategy but additional risks would not feed in separately.	,	Don't publish
5	Chapter 5	5.1	3	19	Amendment	As per comment on Expectation 2.2, the wording should be changed to “business and risk strategies”.	See above	,	Don't publish

6	Chapter 5	5.1	3.1	19	Amendment	The wording should reflect that no single board member but the board collectively are responsible. The wording should also reflect that board members collectively should have adequate knowledge.	While a board member can be responsible for a functional area, all board members have joint and several liability for all risks to which the bank is exposed. The second amendment is appropriate as it is inadequate to expect full knowledge on each issue from each individual board member.	,	Don't publish
7	Chapter 5	5.1	3.2	20	Amendment	As per the comments on Expectation 2.2, this creates significant changes to current processes and will need a staggered approach to embed. The wording should also be changed to “business and risk strategies”.	See above	,	Don't publish
8	Chapter 5	5.1	3.3	21	Amendment	The wording should reflect that the oversight role of the executive management is the responsibility of the supervisory function.		,	Don't publish
9	Chapter 5	5.2	4.2	21	Amendment	Financial institutions already use a range of qualitative metrics. Therefore, the ECB should start with the usage of these, which institutions can align with their current practices and existent information from their clients. Over time, banks can complement the qualitative metrics with quantitative ones. At present, banks are lacking comprehensive climate related data from clients, at least for a large portion of portfolios, these are therefore not implementable in the short order. Without giving guidance on how to derive these (e.g. standard metrics to be used), there is the risk that this expectation cannot be fulfilled by all banks in a satisfactory manner. We suggest that the ECB initiates a collective process for the industry to develop these metrics to ensure practical relevance through working groups or similar formats (please refer to our comment on industry-coordinated work in section 1). The wording should reflect the fact that climate related metrics are being developed currently, but may not be available for large parts of the portfolio at the end of 2020.		,	Don't publish
10	Chapter 5	5.2	4.3	23	Clarification	We understand that the ECB expects relevant metrics and KPIs to be implemented when developed, meaning by end of 2021.		,	Don't publish
11	Chapter 5	5.3	5	23	Amendment	The wording should refer to “internal control framework, e.g. the three lines of defence model” .	This is a widely used model but not mandatory to use.	,	Don't publish

12	Chapter 5	5.3	5.1	24	Amendment	This expectation should be formulated in a less prescriptive way and closer to the contents of the TCFD recommendations.	This Expectation should be rephrased to make it principle-based, rather than prescriptive in terms of processes and working procedures. Banks are currently developing climate-related metrics. A full integration into business and risk strategies remains dependent on further progress in the development of climate and environmental risk frameworks.	,	Don't publish
13	Chapter 5	5.3	5.3	24	Amendment	We refer to our comment on Expectation 5; the wording should be aligned accordingly here.	See above	,	Don't publish
14	Chapter 5	5.3	5.5	25	Amendment	The Expectation should reflect that the role of the compliance function in the context of ensuring adherence to sustainability related applicable laws, rules, regulations and standards can only be the same one concerning identifying, assessing, measuring, monitoring and reporting as it has been so far for other relevant regulation.		,	Don't publish
15	Chapter 5	5.3	5.6	25	Amendment	The Expectation should reflect that the ways in which assurance is provided for the organisation is up to the individual internal audit function.	The draft seems to be limiting internal audit to reviewing climate/environmental risks inside of a risk management review.	,	Don't publish
16	Chapter 5	5.6	6.1	26	Amendment	Full implementation should be synchronised with the outcomes of the revision of the non-financial reporting framework by the European Commission in 2021. Only when the consequent legislation is in place and the data streams are established, this Expectation can be fully operational.	The metrics contained in this Expectation are dependent on disclosures by clients as explained in the response to expectation 4.2.	,	Don't publish
17	Chapter 5	5.6	6.2	26	Amendment	The ECB should acknowledge that required amendments and upgrades to IT systems take time to build. The wording should reflect the fact that banks are in the development phase that may not be complete before 2022.		,	Don't publish
18	Chapter 5	5.6	6.4	27	Amendment	The Expectation should reflect that, for the time being, information will be provided as a best-effort extrapolation of less-frequently aggregated data due to the unavailability of daily aggregated data.	As per our response to Expectation 6.2, the IT systems for this may not be complete before 2022.	,	Don't publish

19	Chapter 6	6.1	7	28	Amendment	The ECB should reflect that this is as an example of topics to give particular attention to rather than to create a specific coverage requirement that may or may not be of heightened relevance for the organisation. Alternatives approaches would be: 1) Use this topic as something that should be considered, and / or 2) Specify that the organisation must consider the extent to which the topic is applicable to them. The default assumptions of both applicability and high risk seems too broad and does not take into account the varying risk profiles of different types of organisations.	Internal audit functions are expected to focus on the highest risks to the organisation and should have the scoping freedom to determine whether climate / environmental risks form part of this risk category for their organisation.	,	Don't publish
20	Chapter 6	6.1	7.1	28	Amendment	It should be made clear that climate-risk is not a stand-alone risk type but an integrated risk.	On the credit risk management side, Expectation 8.1 says that “institutions are expected to form an opinion on how risks affect the borrower’s default risk”. Yet this Expectation would give institutions the possibility of treating climate-related risks as a stand-alone risk type	,	Don't publish
21	Chapter 6	6.1	7.3	29	Amendment	This Expectation should reflect the fact that climate-related metrics are still being developed. Full integration into business and risk strategies remains dependent on progress in such projects, making a phased approach necessary.		,	Don't publish
22	Chapter 6	6.1	7.4	30	Amendment	The wording should: (1) emphasise the importance to differentiate by sector and, potentially, location, meaning to (i) develop sector-specific policies/regional approaches; (ii) engage with clients; and (iii) undertake enhanced due diligence (including escalation to committee) only for clients/transaction that have material environmental and/or climate related risk, and (2) define exposure thresholds for the proposed risk assessment and enhanced due diligence, to limit the analysis to exposures that have some significance. Especially SMEs and non-EU-based clients will not have disclosure requirements, making it very challenging for banks to conduct climate-related and environmental due diligence in these cases. Moreover, it remains unclear how client categories such as banks and sovereigns are to be treated.	Running this type of due diligence for every client relationship is not adequate, as comprehensive data is not readily available in many sectors and sizes of business.	,	Don't publish
23	Chapter 6	6.1	7.5	31	Amendment	As they serve as a quasi-standard for banks, the ECB should align this Expectations more closely with the contents of the TCFD recommendations.		,	Don't publish

24	Chapter 6	6.2	8.1	32	Amendment	Whilst we agree with the inclusion of climate-related and environmental risks in all stages of the credit-granting process and credit processing, a prescriptive requirement to make these risks mandatory risk drivers of all rating models (in particular IRB Rating models) is not adequate. Such an expectation would be far too ambitious given the lack of climate-related risk data available. There is an even wider gap on availability and institutional operationalisation of environmental standards. Instead, the potential impact from climate-related and environmental risks on borrower risks could be assessed on portfolios of borrowers instead of individual assessment. For example, mortgagees in flood lands could be flagged with a “heightened default risk” flag, thereby providing transparency but also an actionable data point as part of the credit approval process. In specific portfolio segments, an expert judgement override could be introduced of a Rating created by an IRB Model. However, this override will not be easily justifiable by historic experience of the bank and therefore face significant obstacles by Model Risk Management as well as by ECB’s model change process. Either way, such introduction of climate-related and environmental risk drivers into IRB Ratings would only be possible from 2022 onwards (after compliance date with EBA PD/LGD guidelines). And likely take many years to get operationalized. Therefore, we propose to explicitly refrain from requiring changes to PD Ratings of the bank at the current stage. If this was not possible, then the guide should include a reference to the proportionality principle, especially for retail portfolios or a transition period for implementing the expectations.	This Expectation runs in parallel with the EBA Guidelines on Loan Origination and Monitoring. This means that the application timeline should be aligned with the in-force date of the Guidelines.	,	Don't publish
25	Chapter 6	6.2	8.4	33	Amendment	This needs to be reviewed, as it is disproportionate to intervene in the pricing framework via a supervisory expectation. There is a potential for unintended consequences, particularly for sectors that face higher challenges to transition into a low-carbon economy and that may be affected by lower credit ratings anyhow, ranging from even higher costs to the risk of “stranded assets”. Moreover, if EU banks were required to adapt their pricing in this way, it would distort the global level playing field. Changing the pricing strategy should be an option for banks but not an obligation or requirement, as we would clearly prefer setting of incentives, rather than additional charges on loan pricing.		,	Don't publish

26	Chapter 6	6.2	8.5	33	Amendment	. The Expectation needs to make provision for such cases and should, for a start, only refer to companies caught in the EU Taxonomy framework or the EU Disclosure Regulation. Moreover, there is no guidance how specific client categories such as banks and sovereigns are to be treated. Moreover, the treatment of new clients seems unclear. A detailed assessment for new clients is usually only possible once the environmental and social due diligence has been completely undertaken. This happens to a large extent after having been mandated for a transaction and having agreed to pricing.	SMEs and non-EU-based clients will not have disclosure requirements, making it very challenging for banks to conduct climate related and environmental due diligence	,	Don't publish
27	Chapter 6	6.4	10	36	Amendment	Enhanced monitoring should only be required for investments that pose a higher environmental risk.	It is reasonable that all portfolios and their underlying products should be assessed to identify any products that pose a higher environmental risk and therefore trigger any enhanced monitoring.	,	Don't publish
28	Chapter 6	6.5	11	37	Amendment	The Expectation should reflect the fact that climate-related metrics are still being developed.	Full integration into capital adequacy remains dependent on further progress in the development of such and additionally environmental risk frameworks. Such an Expectation cannot be fulfilled immediately and should therefore be phased in.	,	Don't publish
29	Chapter 6	6.6	12	38	Amendment	Please refer to our comment to Expectation 11.		,	Don't publish
30	Chapter 7	7.1	13.1	40	Amendment	The ECB should align the wording more closely with the EBA and TCFD standards, as these are already being operationalised.	Although the Expectation references the EBA Guidelines on materiality, proprietary and confidentiality and on disclosure frequency and the TCFD recommendations, it seems to go beyond their contents by specifying required internal procedures, specifically in terms of materiality assessment.	,	Don't publish
31	Chapter 7	7.1	13.2	41	Amendment	The wording of this Expectation should recognize the fact that quantitative climate-related metrics are under development at present. This means quantitative information on materiality is limited to some extent. The Expectation should either be confined to qualitative information or provide a phase-in period for the introduction of additional quantitative metrics.		,	Don't publish
32	Chapter 7	7.1	13.3	41	Amendment	A phase-in period to fulfil such additional requirements will be necessary.	As per our two comments above, this goes beyond the preparations many banks are making to implement the TCFD recommendations	,	Don't publish

33	Chapter 7	7.1	13.5	43	Amendment	Wording should reflect that fact that climate related databases are being built, along with climate related metrics, but will not be available for large parts of the portfolio at the end of 2020. This Expectation should either only gain force once the data is available, or it should be limited to a best-efforts basis.	Disclosure of overall group Scope 3 emissions is not achievable immediately – the necessary data streams are still being built.	,	Don't publish
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