Regulatory Alert

Regulatory Insights

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Board Action: Climate Risk Questions for Management

To promote and accelerate improvements in climate risk management practices at large banks, the OCC outlines key questions that boards of directors should be asking of senior management related to climate change and associated financial risks.

The OCC has outlined five key questions that boards of directors should be asking related to climate change and financial risks.

1. **What is our overall exposure to climate change?**
   - Understanding overall exposure requires senior managers to develop a framework, risk taxonomy, key metrics, datasets, a balanced approach to scenario analyses, and expertise on the portfolio impacts of physical and transition risks.

2. **Which counterparties, sectors, or locales warrant our heightened attention and focus?**
   - Climate change presents both physical and transition risks that could significantly impact the creditworthiness of some borrowers or sectors
   - *Physical risks* include the increased frequency, severity, and volatility of extreme weather and long-term shifts in global weather patterns and their associated impact on the value of financial assets and creditworthiness
   - *Transition risks* relate to the adjustment to a low-carbon economy and include associated changes from government policy, technology, and consumer and investor sentiment.

3. **How exposed are we to a carbon tax?**
   - OCC states that while the United States is not likely to adopt a carbon tax in the near future, banks are recommended to perform scenario analyses where one is implemented, enabling the board to see significant exposures or concentrations of risk. OCC says, "the estimate itself, the exercise of coming up with a number will require processes, data, and calculations that will strengthen transition risk measurement practices more broadly."

4. **How vulnerable are our data centers and other critical services to extreme weather?**
   - Banks should update business continuity and disaster recovery plans to incorporate the full range of climate scenarios into risk assessment and mitigation measures, including consideration of impacts to third-party vendors.

5. **What can we do to position ourselves to seize opportunities from climate change?**
   - Optimize climate risk management systems and capabilities in order to better withstand climate change events and take advantage of opportunities that arise. For example, renewables, carbon capture, electric vehicles, and charging stations will create banking opportunities. Changes in agriculture, water

infrastructure, consumer preferences, and investor sentiment will also create opportunities.

Forthcoming guidance

In addition to providing this guidance, the Acting Comptroller reported that the OCC is currently developing high-level supervisory expectations for large banks related to climate risk management and expects to issue framework guidance by the end of 2021. This framework will be followed with detailed guidance for each risk area in 2022.

Please also refer to these KPMG Regulatory Insights Regulatory Alerts:

— FSOC issues climate risk recommendations
— Take-aways from COP26 Finance Day
— Climate Reporting: Recent Updates Impacting Financial Services
— Climate Risk Modeling: Scenario analysis

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