Regulatory Alert

Regulatory Insights

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FSOC issues climate risk recommendations

Key points

The FSOC's report stresses the importance of coordination among the financial regulators and with their international counterparts to meaningfully accelerate a consistent approach to managing climate-related risks while also highlighting the regulators' progress and ongoing efforts to address these risks within their jurisdictional authorities. Key recommendations touch on issues of current regulatory concern including eliminating data gaps, enhancing and standardizing disclosures, and developing management tools such as scenario analysis.

The Department of the Treasury's Financial Stability Oversight Council (FSOC) has released a report on Climate-Related Financial Risk, as required by Executive Order 14030 signed in May 2021. (*See KPMG Regulatory Alert here*.)

The FSOC identifies climate change as an emerging threat to the financial stability of the United States and states that it is the responsibility of the FSOC to ensure the resiliency of the U.S. financial system to climate-related financial risks. The report is deemed a "first step," representing an initial review of the current efforts by FSOC members to incorporate climate-related financial risk into their regulatory and supervisory activities, enhance climate-related disclosures, and assess climate-related risks to U.S. financial stability. Multiple recommendations under four overarching themes are intended to serve as a coordinated and accelerated agenda for the FSOC members as they work to promote resilience and help support an orderly, economy-wide transition toward the Administration's goal of net-zero emissions by 2050.

The key recommendations include:

— **Building capacity and expanding efforts to address climate-related financial risks.** This includes:
  - Forming a Climate-related Financial Risk Committee (CFRC) and underlying advisory committee to identify priority areas and serve as a coordinating body for information sharing, developing approaches and standards, and facilitating communications.
  - Prioritizing members' internal investments to expand capacity to define, identify, measure, monitor, assess, and report on climate-related financial risks and their effects on financial stability, including investments in staffing training, expertise, data, analytic and modelling methodologies, and monitoring.

— **Filling climate-related data and methodological gaps,** by:
  - Promptly identifying and taking next steps to ensure consistent and reliable data for assessing climate-related risks, including inventorying

currently collected and procured data and developing plans to obtain additional data.
  - Developing consistent data standards, definitions, and relevant metrics.
  - Coordinating with international regulatory counterparts regarding data gaps, definitions, standards, metrics, and tools.

— **Enhancing public climate-related disclosures.** FSOC recommends the members:
  - Update disclosure requirements to promote consistency, comparability, and the decision-usefulness of information on climate-related risks and opportunities.
  - Standardize data formats to promote comparability, such as the use of structured data using the same or complementary protocols.
  - Consider building on the core elements of the Financial Stability Board's Task Force on Climate-related Financial Disclosure (TCFD) "to the extent consistent with the U.S. regulatory framework and the needs of U.S. regulators and market participants."
  - Consider whether disclosures should include greenhouse gas (GHG) emissions.

— **Assessing and mitigating climate-related risks that could threaten the stability of the financial system**. This would include:
  - Collaborating with external experts to identify climate forecasts, scenarios, and other tools necessary to better understand the exposure of regulated entities to climate-related risks and how those risks translate into economic and financial impacts.
  - Coordinating with international regulatory counterparts.
  - Using scenario analysis, taking into account supervisory and regulatory mandates and the size, complexity, and activities of the regulated entities.

Impact on vulnerable populations

The report highlights that adverse effects of climate change are likely to disproportionately impact financially vulnerable communities, including low-income communities, communities of color, and other disadvantaged or underserved communities. The FSOC specifically recommends that its members coordinate the analysis of climate-related financial risks conducted in their supervisory and regulatory functions with efforts to understand the impacts on communities and households. Further, the members are encouraged to evaluate climate-related impacts and the impacts of proposed policy solutions on financially vulnerable populations when assessing the impact of climate change on the economy and the financial system. (*See KPMG Regulatory Alert on Climate Equity, here*.)

Net-zero emissions

The FSOC notes that the United States has committed to lowering U.S. GHG emissions by 50-52 percent by 2030 (from 2005 levels) and set a goal of net-zero emissions by 2050. It states that meeting these targets will require significant changes across the economy, especially in GHG-intensive sectors. The changes may require technological innovations and complementary policy actions to incentivize transitions to low-GHG methods of production, and may broadly affect households, communities, and businesses.

Relevant links:
— KPMG Regulatory Insights Regulatory Alerts
— KPMG IMPACT: Your ESG solution

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