

February 6, 2023

Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, DC 20551



Japanese Bankers Association

JBA comments on the draft Principles for Climate-Related Financial Risk Management for Financial Institutions proposed by the Board of Governors of the Federal Reserve System

Dear Sirs/Madams:

Introduction

The Japanese Bankers Association¹ (the “JBA”) appreciates the opportunity to comment on the draft Principles for Climate-Related Financial Risk Management for Financial Institutions² (hereafter “the Principles”) proposed by the Board of Governors of the Federal Reserve System (the “Board”), which provide a high-level framework for the safe and sound management of exposure to climate-related financial risks.

We welcome that the Principles are broadly consistent with the Principles for the effective management and supervision of climate-related financial risks³ by the Basel Committee on Banking Supervision (hereafter “the BCBS Principles”), which will be a common baseline for internationally active banks and supervisors. We also welcome the Board’s consistent approach and implementation timeline with other U.S. agencies, including the Office of the Controller of the Currency (the “OCC”) and the Federal Deposit Insurance Corporation (the “FDIC”).

Regarding our views on approaches for achieving greater coordination, please refer to the comments submitted by the JBA to the OCC’s draft Principles for Climate-Related Financial Risk Management for Large Banks, which is attached to this letter (the “JBA comments to the OCC”). We welcome the clarification that has been added to the Principles - based on feedback through consultation with the OCC and the FDIC - on the calculation of total consolidated assets of the branches or agencies of foreign banking organizations to which the Principles will apply and on the role of the board and senior management.

Interoperability of US and international standards

Our member banks are in the process of implementing a climate-related financial risk management framework at a group-wide level, engaging with the relevant regulators and we would appreciate further clarification on how this applies to FBOs as stated below in our response to Question 1. If financial institutions with global operations are required to comply with all the different guidelines in each jurisdiction, it would lead to ineffective risk management and a burden for banks. In order to avoid duplicative or different requirements for banks, we would like to ask the Board to continue to coordinate with international standard setting bodies and jurisdictional supervisors. We would propose an interoperable approach where non-U.S. banks with U.S. operations can rely on and comply with the guidelines in their home country to the extent they are consistent with the BCBS Principles and broadly aligned with the future Board’s guidance. For the same reason of avoiding duplicative or different requirements, we also encourage the Board to coordinate with foreign regulators to harmonize supervisory expectations to the greatest extent possible.

¹ The Japanese Bankers Association is the leading trade association for banks, bank holding companies and bankers associations in Japan. As of February 6, 2023, the JBA has 114 Full Members (banks), 3 Bank Holding Company Members (bank holding companies), 76 Associate Members (banks & bank holding companies), 51 Special Members (regionally-based bankers associations) and one Sub-Associate Member for a total of 245 members. Several of its largest member banks are active participants in the U.S. financial markets.

² <https://www.federalreserve.gov/newsevents/pressreleases/other20221202b.htm>

³ <https://www.bis.org/press/p220615.htm>

Challenges in climate risk management

When incorporating climate-related financial risks into existing risk management, such as credit ratings and credit costs, there are a number of challenges, including different time horizons (an extremely long term for climate-related financial risks, which contrasts with current horizons used for existing risk management), and a lack of availability and credibility of data (such as data on the relationship between climate-related risks and credit losses). Therefore, we recognize that it will require a considerable amount of time to establish quantitative financial risk management practices at the client level. Given such data challenges and the evolution of climate risk measurement methodologies/modelling, the future Board's guidance needs to be flexible and principle-based. We would like the Board to provide sufficient time for implementation of the future Board's guidance, incorporating the progress of international discussions and allowing us to take a phased approach to implementation.

Incorporating climate-related risks into capital or liquidity adequacy assessments

Due to the current limitations in terms of data and methodologies/modelling stated above, we believe that it would also be premature to include an expectation that banks incorporate climate-related financial risks into their capital and liquidity adequacy assessments at this point in time. We appreciate that the Board recognizes such challenges regarding data and methodologies in the Principles and believe that it should be reflected in the Board's final Principles. We also welcome the Board's approach taken in the Participant Instructions for the Pilot Climate Scenario Analysis Exercise⁴ that climate scenario analysis is distinct and separate from bank stress tests and that the pilot climate scenario analysis exercise is exploratory in nature and does not have capital consequences. We believe that guidance by the Board in the future should also take the same approach.

Response to the questions

Question 1: In what ways, if any, could the draft principles be revised to better address challenges a financial institution may face in managing climate-related financial risks?

We would like to ask the Board to:

- Clarify how this applies to FBOs, with examples of when the threshold of \$100 billion would be considered met and how the principles should be implemented across various corporate structures at FBOs.
- Clarify if any principles must be met locally by FBOs as opposed to globally through organization-wide policies and processes and to ensure alignment with requirements in foreign jurisdictions.
- Define a compliance approach that accounts for the time required by banks to implement the climate-related financial risk management processes outlined in the principles and incorporate climate-related financial risks into decision-making processes. Provide a period for banks to demonstrate progress, rather than set a particular data for compliance.

Please also refer to the JBA comments to the OCC on Questions 2 and 6.

Question 2: Are there areas where the draft principles should be more or less specific given the current data availability and understanding of climate-related financial risks? What other aspects of climate-related financial risk management, if any, should the Board consider?

In the area of climate-related risks for which standard practices have not been established, it is necessary to quantify specifically the elements required to conduct scenario analysis. In addition, it is important that specific elements of such measures are consistent with other countries/regions.

In addition, the principles proposed by the Board will need to consider how to estimate climate-related financial risk in situations where firm-level climate data are constrained.

Commercial banks have a wide range of customers and types of financial instruments. Therefore, it is extremely

⁴ <https://www.federalreserve.gov/newsevents/pressreleases/other20230117a.htm>

difficult to monitor all transactions after the first disbursement of a loan (e.g. rollover of the short-term credit facility that hits materiality due to the amount). The principles to be proposed by the Board should clearly specify the scope of risk management.

The incorporation of examples and best practice criteria and/or case studies, including the above aspects, would help organizations to understand and meet the requirements.

Please also refer to the JBA comments to the OCC on Question 10.

Question 3: What challenges, if any, could financial institutions face in incorporating these draft principles into their risk management frameworks?

We believe that the following challenges need to be addressed:

- Lack of clear and robust data coverage across the portfolio
- Lack of consensus on approach/methodology for analysis, particularly scenario analysis
- Lack of sufficient time to implement policies and procedures

In particular, in order to address challenges on data availability and credibility, we believe that it is important to build a system infrastructure for climate data analysis. It is also important to establish and share assumptions and methodologies as a preliminary step in conducting risk management and analysis in areas where there is a lack of common consensus.

Please also refer to the JBA comments to the OCC on Question 3.

February 14, 2022

Office of the Comptroller of the Currency
400 7th St. SW
Washington, DC 20219



Japanese Bankers Association

JBA comments on the Office of the Comptroller of the Currency's draft Principles for Climate-Related Financial Risk Management for Large Banks

Dear Sirs/Madams:

The Japanese Bankers Association⁵ (JBA) appreciates the opportunity to comment on the Office of the Comptroller of the Currency's (OCC) draft Principles for Climate-Related Financial Risk Management for Large Banks⁶ (hereafter "the Principles"), which provide a high-level framework for the safe and sound management of exposure to climate-related financial risks.

We welcome that the OCC's Principles are broadly consistent with the proposed principles⁷ by the Basel Committee on Banking Supervision (hereafter "the BCBS Principles"), which will be a common baseline for internationally active banks and supervisors. We encourage the OCC to promote a domestically consistent approach as well with other U.S. agencies, including the Federal Reserve Board.

Our member banks are in the process of implementing a climate-related financial risk management framework at a group-wide level, engaging with the relevant regulators. If financial institutions with global operations are required to comply with all the different guidelines in each jurisdiction, it would lead to ineffective risk management and a burden for banks. In order to avoid duplicative or different requirements for banks, we would like to ask the OCC to continue to coordinate with international standard setting bodies and jurisdictional supervisors. We would propose an interoperable approach where non-U.S. banks with U.S. operations can rely on and comply with the guidelines in their home country to the extent they are consistent with the BCBS Principles and broadly aligned with the future OCC guidance. For the same reason of avoiding duplicative or different requirements, we also encourage the OCC to coordinate with foreign regulators to harmonize supervisory expectations to the greatest extent possible.

When incorporating climate-related financial risks into existing risk management, such as credit ratings and credit costs, there are a number of challenges, including different time horizons (an extremely long term for climate-related financial risks, which contrasts with current horizons used for existing risk management), and a lack of data availability and credible data (such as data on the relationship between climate-related risks and credit losses). Therefore, we recognize that it will require a considerable amount of time to establish quantitative financial risk management practices at the client level. Given such data challenges and the evolution of climate risk measurement methodologies/models, the future OCC guidance needs to be flexible and principle-based. We would like the OCC to provide sufficient time for implementation of the future OCC guidance, incorporating the progress of international discussions and allowing us to take a phased approach to implementation.

Also due to the challenges stated above, we believe that it will also be premature to include an expectation that banks incorporate climate-related financial risks into their capital and liquidity planning processes at this point in time, and that further data and development of quantitative tools and methodologies is needed.

⁵ The Japanese Bankers Association is the leading trade association for banks, bank holding companies and bankers associations in Japan. As of February 14, 2022, JBA has 114 Full Members (banks), 3 Bank Holding Company Members (bank holding companies), 77 Associate Members (banks & bank holding companies), 58 Special Members (regionally-based bankers associations) and one Sub-Associate Member for a total of 253 members. Several of its largest member banks are active participants in the U.S. financial markets.

⁶ <https://www.occ.treas.gov/news-issuances/bulletins/2021/bulletin-2021-62a.pdf>

⁷ Basel Committee on Banking Supervision, *Consultative Document: Principles for the effective management and supervision of climate-related financial risks*
<https://www.bis.org/bcbs/publ/d530.pdf>

Comments on the General Principles

Strategic Planning

Given a lot of uncertainty around climate-related financial risks and data gaps, it will take a reasonable amount of time to fully incorporate climate-related financial risks into business strategy and capital/risk appetite. We would like to ask the OCC to allow banks to integrate climate-related financial risks into strategic planning based on the data and methodologies that are available at this stage.

Scenario Analysis

We welcome the approach taken by the Principles, which recognize the distinction between scenario analysis and traditional stress testing based on their different purposes. We believe that the future OCC guidance also needs to clearly differentiate between scenario analysis and stress testing.

We also support the idea that “management should develop and implement climate-related scenario analysis frameworks in a manner commensurate to the bank’s size, complexity, business activity, and risk profile” as stated in the Principles.

Comments on the Management of Risk Areas

Liquidity Risk, Other Financial Risk, Operational Risk, Legal/Compliance Risk, Other Nonfinancial Risk

Further work will be necessary to understand the relationship between climate-related financial risks and liquidity risk, market risk, operational risk, and other financial/nonfinancial risk. In particular, we should achieve a consistent and common understanding (measurement or methodology) of the transmission channel from the risk driver of climate-related financial risks to each risk. Therefore, it might be premature at this stage to require banks to incorporate specific risk mitigation tools for those risks in the future OCC guidance. We would like the OCC to secure enough time to take these risks into consideration, and allow us to apply different time horizons for each risk category when implementing the guidance.

Response to the questions

Applicability

1. Are there additional categories of banks (i.e., based on asset size, location, business model) to which these principles should apply?

The Principles set out that they are targeted at banks with over \$100 billion in total consolidated assets. However, we believe that the scope of application of the future OCC guidance needs to consider not only asset size, but also to “reflect differences in banks’ circumstances such as complexity of operations and business models” in a comprehensive manner, as many factors can lead to material exposure to climate-related financial risks for banks.

We agree that “all banks, regardless of size, may have material exposures to climate-related financial risks” as stated in the Principles. Therefore, we would like the OCC to clarify the rationale to apply the Principles only to large banks, and clarify that the definition of “over \$100 billion in total consolidated assets” for non-U.S. banks mean over \$100 billion in total consolidated assets in the U.S. rather than at the whole enterprise level. At the same time, we believe that it is not appropriate to apply the same guidance both to “U.S. banks with over \$100 billion in total assets” and to “non-U.S. banks with combined U.S. assets of over \$100 billion” and that the OCC should consider the circumstances and exposure to climate-related financial risks of the U.S. operations of non-U.S. banks in applying the Principles and future OCC guidance.

As noted above, we would also like to ask the OCC to collaborate with the Federal Reserve Bank to harmonize supervisory expectations for U.S. banks, so that all banks in the same circumstances will be subject to the same

supervisory expectations.

Tailoring

2. How could future guidance assist a bank in developing its climate-related financial risk management practices commensurate to its size, complexity, risk profile, and scope of operations?

Since globally consistent standards for addressing climate-related financial risks and appropriate risk management methodologies have not been established at present, we would like for the future OCC guidance to take a principle-based and flexible approach to enhance climate-related financial risk management practices going forward.

Also, if the future guidance could provide good practices or case studies, it would help banks to enhance our capabilities for effective climate-related financial risk management.

We would welcome further opportunities for additional review before the OCC finalizes the future guidance.

General

3. What challenges do banks face in incorporating these principles into their risk management systems? How should the OCC further engage with banks to understand those challenges?

As stated above, due to a lack of a common consensus on methodologies and monitoring/reporting metrics, our member banks have been trying to explore how to develop a management framework on climate-related financial risks. Other challenges include a limitation on data for analysis and the establishment of a data system infrastructure. Therefore, we would appreciate it if public sectors and private sectors could jointly address these challenges, and we would like the OCC to consider providing sufficient time for the development of a risk management framework by banks.

Current Risk Management Practices

4. What specific tools or strategies have banks used to successfully incorporate climate-related financial risks into their risk management frameworks?

For example, some member banks are using and developing the Risk Appetite Framework and quantitative metrics (KPIs/KRIs) and scenario analysis on credit risk and market risk. They have disclosed the impact of transition risks and physical risks in the risk management area in their annual report and sustainability report aligned with the Task Force on Climate-related Financial Disclosures (TCFD) framework.

5. How do banks determine when climate-related financial risks are material and warrant greater than routine attention by the board and management?

Some member banks have developed and implemented a sound process for understanding and assessing climate-related financial risks. For example, one member bank has recognized climate-related risks as top risks in its existing risk management framework, and regularly reported the financial impact of climate-related risks to the Risk Management Committee under the control of the Board of Directors and the Risk Management Committee and the Investment and Finance Committee, which are the committees of the Executive Committee.

It has also put in place a global and group framework where the chief risk officers in its group companies can share and discuss measures to address climate-related risks.

6. What time horizon do banks consider relevant when identifying and assessing the materiality of climate-related financial risks?

A clear common view of which time horizon is relevant has not been established, as they are still under consideration globally. For example, when incorporating climate-related financial risks into existing frameworks, such as credit ratings, consideration of different time horizons has not reached an international

consensus. The future OCC guidance should allow for appropriate, risk-based flexibility across its supervisory expectations (e.g., scenario analysis and strategic planning) to account for significant variability over longer time horizons.

In addition, although it is necessary to measure long-term risks, it is very difficult to predict how society as a whole will transition to a low-carbon economy or how each corporate will change its business in the long-term. It should be noted that when and how much risk appears depend on the assumptions and presumptions by each bank, and therefore it is the variation in measurement might be large. Therefore, we would like international standard setting bodies and jurisdictional supervisors to clarify the concept of the time horizon for measurement as much as possible, recognizing the need to balance these expectations with each bank's discretion to make its own risk-based determinations.

7. What, if any, specific products, practices, and strategies—for example, insurance or derivatives contracts or other capital market instruments—do banks use to hedge, transfer, or mitigate climate-related financial risks?

For project finance transactions, in general, physical damage from climate change (e.g. earthquake, flood, windstorm, etc.) is mitigated through insurance.

8. What, if any, climate-related financial products or services—for example, “green bonds,” derivatives, dedicated investment funds, or other instruments that take climate-related considerations into account—do banks offer to clients and customers? What risks, if any, do these products or services pose?

For example, our member banks provide the following products:

- (i) Green loans, a loan product that finances eligible green projects such as investment in solar or wind power.
- (ii) Social loans, a loan product that finances eligible social projects such as investment in the operation of hospitals or affordable housing. Social loans can be utilized for climate change adaptation through projects related to disaster response and preparedness.
- (iii) Sustainability loans, a loan product that is a combination of social and green projects as described above.
- (iv) Sustainability-linked loans (SLL), a loan product that sets sustainability performance targets (SPT) based on a customer's ESG strategy. The terms of the loan change depending on the achievement of the target. SLLs can take climate related considerations into account when the SPT is related to climate change mitigation or adaptation.
- (v) Transition loans, a loan product that supports the transition of corporations from high to low GHG emissions if the corporation has a transparent transition strategy (including targets) and appropriate governance structure to support that transition.
- (vi) Positive impact finance (PIF), a loan product that evaluates the social, environmental, and economic impact of a corporation's business and evaluates whether or not the corporation is working to increase its key positive impacts and reduce its key negative impacts. Both positive and negative impact areas can be related to climate change.

Most of the above products are provided in alignment with existing principles provided by the International Capital Markets Association (ICMA), Loan Market Association (LMA), or United Nations Environment Programme Finance Initiative (UNEP FI).

9. How do banks currently consider the impacts of climate-related financial risk mitigation strategies and financial products on households and communities, specifically LMI and other disadvantaged communities?

We agree that it is important for banks to take into account the impact of climate-related financial risks on LMI and other disadvantaged households and communities. We would seek further clarification on the OCC's expectations in this area.

Data, Disclosures, and Reporting

10. What, if any, specific climate-related data, metrics, tools, and models from borrowers and other counterparties do banks need to identify, measure, monitor, and control their own climate-related financial risks? How do banks currently obtain this information? What gaps and other concerns are there with respect to these data, metrics, tools, or models?

Our member banks obtain specific data, such as climate-related variables, industry-specific variables, and the amount of GHG emissions of individual firms, from vendors and public databases. A major concern with respect to such data, metrics, tools, or models is the gap between firms' disclosures/strategies and the results of scenario analysis.

As an example, banks recognize that carbon footprint is a useful source of information for their decision-making, as well as communication with stakeholders (e.g. investors). Therefore, banks would like to estimate CO₂/GHG emissions from their portfolio as soon as possible.

On the other hand, there are still many companies that do not collect or disclose their carbon footprint (Scope 1, 2 and 3). We also recognize that global standards for estimating carbon footprint have not yet been established. So, the current situation is that each financial institution is still conducting research for the introduction of standardized or consistent data. In such a situation, it is true that accurate risk measurement is difficult.

The above-mentioned challenges could be solved by (i) the standardization of metrics related to carbon footprint measurement and/or (ii) the disclosure of carbon footprint reference data for each sector by governments/regulators. We would like to ask the OCC to continue to coordinate with international standard setting bodies and jurisdictional supervisors to standardize metrics and/or to encourage governments to disclose relevant data, as these activities are expected to boost disclosures for banks.

Also, in order to obtain detailed output through scenario analysis, etc., elaborate management plans (for example, how to deal with climate-related risks) of corporate clients are required from the perspective of understanding long-term transition risks. Since the collection of these plans is likely to be very burdensome and time-consuming, we would like to ask for flexibility on the scope of risk measurement (for example, which industries or sectors should be targeted for risk measurement, etc.).

We need a consistent and common understanding (measurement or methodology) for a transmission channel from the risk driver of climate-related financial risks, although we understand that the BCBS report published in April 2021⁸ mentions the transmission relationship. A common approach would bring about enormous benefits, such as accelerating the risk assessment process in financial institutions and allowing comparison and benchmarking across the global financial system.

11. How could existing regulatory reporting requirements be augmented to better capture banks' exposure to climate-related financial risks?

We would like the OCC to leverage existing regulatory reporting requirements. Existing securities regulatory disclosure regimes need to be leveraged regarding banks' exposure to climate-related financial risks.

Scenario Analysis

12. Scenario analysis is an important component of climate risk management that requires assumptions about plausible future states of the world. How do banks use climate scenario models, analysis, or tools and what challenges do they face?

Standardized climate scenarios are used to analyse the climate impact on borrowers' financial statements, and any missing variables are obtained from other sources. It is difficult to set assumptions regarding possible technological developments and the investments of each firm based on such developments, and there is a limit to incorporating firm-specific factors into the analysis.

At present, we understand that there is no established methodology for quantifying climate-related risks, such as a VaR measure. It will take time to develop agreed-upon standards and methodologies.

⁸ Basel Committee on Banking Supervision, *Climate-related risk drivers and their transmission channels*
<https://www.bis.org/bcbs/publ/d517.pdf>

13. What factors are most salient for the OCC to consider when designing and executing scenario analysis exercises?

We would like the OCC to consider that uncertainties both in climate-related variables and macroeconomic variables will increase as the time horizon becomes longer. Therefore, due care would be required when analysing the results of scenario analysis.

In all risk area, where standard practices have not been established, the direction of quantification methodologies for executing scenario analysis exercises needs to be indicated.

As proposed in Recommendation 4.4 of the “*Report on Climate-Related Financial Risk*” published in October 2021 by the Financial Stability Oversight Council (FSOC)⁹, we agree to using existing common scenarios, such as scenarios developed by the Network of Central Banks and Supervisors for Greening the Financial System (NGFS), and therefore it would not be necessary for the OCC to develop its own scenarios.

(End)

⁹ <https://home.treasury.gov/system/files/261/FSOC-Climate-Report.pdf>