May 14, 2020

Members of the Climate-Related Market Risk Subcommittee
Commodity Futures Trading Commission
1155 21st St NW
Washington DC 20581

Re: Request for comments from the CFTC's Climate-Related Market Risk Subcommittee

Dear Members of the Subcommittee:

Amazon Watch, a nonprofit organization that advocates for human rights, corporate accountability, preservation of the Amazon's ecological systems, and a livable climate, is pleased to present input to the Subcommittee for its upcoming report.

Risks to the financial system from fossil fuel and deforestation-linked investments

Climate change is already underway, and extensive scientific evidence demonstrates that its impacts are nonlinear and largely unpredictable - they will grow exponentially but we don't exactly know how severe they will be nor in what ways they will manifest.

The impacts of climate change on investments are beginning to be acknowledged by the financial industry. For example, a 2019 BlackRock and Rhodium report acknowledged that climate change is having financial consequences on US securities, investors underestimate these impacts, and climate risk will grow without significant changes, resulting in major instability to our financial system.

However, while it is necessary to evaluate climate risk and climate impacts, measurement and analysis are insufficient given the urgency and scale of the problem: investment firms must also change their relationship to the companies whose emissions are driving climate change, by either divesting or leveraging shareholder power to align capital with a 1.5C world and prevent major economic and financial system crises.

The primary set of commodities at issue are fossil fuels -- the burning of coal, oil, and "natural" gas is the principal causes of climate change. If burned, the world's remaining proven fossil fuel reserves will consume over four times the budget for staying below 1.5C. Deforestation-risk commodities, in turn are the second biggest drivers of climate change and also merit action.

Political and economic responses to this imperative -- in the form of climate policies that disincentivize carbon emissions and production and that accelerate the transition to renewable energy -- put the physical capital of coal, oil, and gas companies at even greater risk of becoming

520 Third Street, Suite 108
OAKLAND, CA 94607
Tel: 510.281.9020 Fax: 510.218.9021

amazon@amazonwatch.org
amazonwatch.org

1101 15th Street NW, 11th Floor
WASHINGTON, DC 20005
Tel: 202.785.8700

stranded. One study estimated that global losses from climate-related stranded assets could amount to US$4 trillion, and identified the U.S. as one of the big losers from those losses. Even before coronavirus hit, fossil fuels were no longer blue chip stocks; they have been among the worst performing sectors of the S&P 500 for a decade now.

A few financial firms – primarily in Europe and Japan - have begun to shift investment practices after acknowledging how their business practices contribute to climate change. U.S. firms, however, continue to draft their feet:

Equity investment in fossil fuels
The fossil fuel holdings of the "big three" asset manager groups – US firms BlackRock, State Street and Vanguard -- alone account for more than 4.75% of 420 Gt CO_2 carbon budget estimated by the October 2018 IPCC report as necessary for maintaining a 66% chance of achieving the 1.5C target. Since the Paris Agreement, the world's largest asset management groups – with a combined $40 trillion in assets – have increased holdings of thermal coal reserves by more than 20%. Though BlackRock made headlines in January with its climate announcement, it has made few changes to its holdings.

Insuring the fossil fuel industry
Not only do insurers cover the risks of coal, oil, and gas companies and projects, they are also significant institutional investors in fossil fuels: according to data reported to the California Department of Insurance in 2017, the 10 largest US insurance companies had $51 billion invested in fossil fuel companies. The insurance industry has already suffered unprecedented losses due to natural disasters in recent years: $140 billion in payouts in 2017 and $80 billion in 2018, compared to a long-term annual average of $41 billion. Additionally, insurers that provide legal liability insurance may be forced to cover some of the damages that fossil fuel companies could be forced to pay as climate change litigation makes progress in the courts.

Lending & underwriting of fossil fuels
Banks directly finance fossil fuel projects, and also provide their fossil fuel-sector clients with financial backing that allows them to continue to expand the fossil fuel industry well outside the bounds of the global carbon budget needed to stay below 1.5C. Between 2016 and 2019, four American banks financed over $800 billion in fossil fuel investments, 30 percent of all global fossil fuel financing. Banks will also suffer losses with mortgages, agricultural loans, and commercial real estate from increased frequency of fires, floods, and hurricanes.

The Role of U.S. Financial Regulators

Climate change poses clear and serious risks to the financial system. U.S. financial regulators have a responsibility to promote financial stability and ensure the normal functioning of the firms and markets under their respective jurisdictions. Regulators have the authority to develop policies to mitigate these climate-related risks. Their statutory mandates require that they focus on this issue because of the risk it poses to the institutions and markets under their purview. Regulators must act now, before irreversible damage is done.

Policy Recommendations

- Improved disclosure: The Securities and Exchange Commission (SEC) should mandate that corporations disclose their exposure to climate risk, their direct level of greenhouse gas emissions, and the emissions of the assets they finance.
- Stress tests: The Federal Reserve and/or the SEC should establish climate risk stress tests for our nation's largest financial institutions, including banks, asset managers, and insurance companies. These tests would help demonstrate the aggregate and individual climate risk exposure of major financial institutions.
- Prudential regulation: Regulators should broadly embed climate risk into their prudential regulatory and supervisory frameworks for systemically important financial institutions, such as capital and margin requirements, supervisory guidance, risk management standards, and potentially portfolio limits.
- Fiduciary duties: The SEC, as well as the Department of Labor, should integrate climate risk into their fiduciary duty frameworks. Investment advisers should have to factor in climate related risks when providing advice to investors.

Sincerely,

Moira Birss
Climate and Finance Director