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New York State Department of Financial Services Encourages Financial Institutions to Consider Risks Associated with Climate Change

WRITTEN BY

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In a letter dated October 29, 2020, Linda A. Lacewell, superintendent of the New York State Department of Financial Services (NYDFS), called on New York state-regulated financial institutions to integrate financial risks from climate change into their governance frameworks, management processes, and business strategies. The NYDFS regulates approximately 1,500 banks and other financial institutions, managing more than $2.6 trillion in assets and nearly 1,800 insurance companies with assets of more than $4.7 trillion. The letter marks the first time an American state or federal regulator has established a set of expectations for financial institutions on managing the financial risks from climate change.

When discussing the motive behind the letter, Ms. Lacewell noted, “We want to ensure that every institution is managing its own individual risks from climate change, which is critical for the safety and soundness of the financial services industry. By working with the industry and engaging in a dialogue on this serious issue, we are creating a roadmap for a more sustainable future.”

The guidance provided in the letter is directed at banking organizations, mortgage companies, trust companies, and non-depositories, including virtual currency, licensed lenders money transmitters, and other financial institutions regulated by NYDFS. Ms. Lacewell stated that she recognizes that these institutions vary in size, complexity, and resources available, and therefore recommends that each institution take a proportionate approach that reflects their individual exposure to the financial risks from climate change.

Two main risks for financial institutions were identified in the letter: transition risk and physical risk. Ms. Lacewell noted that transition risk relates to the market shifts away from fossil fuel-based energy and the risks of investing in stranded assets that may result in losses. Physical risk relates to damage to physical assets that may result from alleged climate-related natural disasters and the resulting supply chain disruptions.

To mitigate these risks, the NYDFS recognizes that traditional risk management processes may not be adequate. One recommendation by the NYDFS is for institutions to designate a board member, a board committee, and a senior management function to focus on the institution’s assessment and management of climate change risks. Additionally, the NYDFS recommends that all regulated institutions consider developing climate-related financial risk disclosure framework.

Ms. Lacewell ended the letter with, “Mitigating the financial risks from climate change is a critical component of creating a stronger industry and a healthier and safer world for ourselves, our families, and future generations.

There is no more time to wait. Let's get to work. Please direct any questions or suggestions regarding this circular letter to Dr. Yue (Nina) Chen, Director of Sustainability and Climate Initiatives, at climate@dfs.ny.gov."

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