To: Senate Special Committee on the Climate Crisis
Re: Why and how addressing the climate crisis requires financial industry regulation
From: Stop The Money Pipeline Coalition

Dear Committee Members,

Thank you for this opportunity to provide input to your deliberations. We write to you from **Stop The Money Pipeline,** a coalition of over 100 organizations around the country working to hold the financial sector accountable for its role in driving the climate crisis and its existing and future impacts on our communities and planet. We respectfully submit the following input, in which we have focused specifically on the reasons why financial industry regulation is crucial to climate action and how lawmakers, regulators, and agencies should take action to ensure financial industry activities are compliant with achieving U.S. and global climate goals.

Introduction

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 know with high precision how severe they will be, nor in what ways they will manifest.[1]

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 U.S. securities, investors underestimate these impacts, and climate risk will grow without significant changes, resulting in major instability to our financial system.[2]

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 1.5ºC world and prevent major economic and financial system crises.[3]

The primary set of commodities at issue are fossil fuels — the burning of coal, oil, and fossil gas is the principal cause of climate change. If burned, the world's remaining proven fossil fuel reserves will consume over four times the budget for staying below 1.5ºC.[4] Burning all coal, oil, and gas reserves already in production would exhaust a 2ºC carbon budget, while burning in-production oil and gas alone

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[1] Marshall Burke, Solomon M. Hsiang & Edward Miguel, "Global non-linear effect of temperature on economic production," *Nature*, 21 October 2015; Christian L. E. Franzke, "Nonlinear climate change," *Nature Climate Change*, 28 May 2014.
[2] *Getting physical: Scenario analysis for assessing climate-related risks*, BlackRock Investment Institute, April 2019.
[3] *Climate Change Threatens the Stability of the Financial System*, Gregg Gelzinis and Graham Steele, 21 November 2019.
[4] IPCC, 2018, "Summary for Policymakers." In "Global Warming of 1.5°C: An IPCC Special Report on the Impacts of Global Warming of 1.5°C Above Pre-Industrial Levels and Related Global Greenhouse Gas Emission Pathways, in the Context of Strengthening the Global Response to the Threat of Climate Change, Sustainable Development, and Efforts to Eradicate Poverty," edited by Valérie Masson-Delmotte et al. World Meteorological Organization, Geneva, Switzerland.

— even if coal is phased out tomorrow — would take us past 1.5ºC.[5] Deforestation-risk commodities, in turn, are the second biggest drivers of climate change and also merit action.[6]

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 stranded.[7] One study estimated that global losses from climate-related stranded assets could amount to $4 trillion, and identified the U.S. as one of the big losers from those losses.[8] 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.[9]

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 drag their feet.

Equity investment in fossil fuels

The fossil fuel holdings of the "Big Three" asset manager groups — U.S. 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 1.5ºC target.[10] 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%.[11] Though BlackRock made headlines in January with its climate announcement, it has made few changes to its holdings as a result, continuing a dangerous industry trend of strong words not being followed by commensurate action.

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 U.S. insurance companies had $51 billion invested in fossil fuel companies.[12] 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

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[5] Kelly Trout, "The Sky's Limit and the IPCC Report on 1.5 Degrees of Warming," Oil Change International, 17 October 2018.

[6] *Climate Change and Land: An IPCC Special Report on climate change, desertification, land degradation, sustainable land management, food security, and greenhouse gas fluxes in terrestrial ecosystems*, IPCC, 2019.

[7] "Stranded Assets," Carbon Tracker Initiative, 23 August 2017.

[8] J.-F. Mercure et al., "Macroeconomic impact of stranded fossil fuel assets," *Nature Climate Change*, 4 June 2018.

[9] Tom Sanzillo and Kathy Hipple, *Fossil Fuel Investments: Looking Backwards May Prove Costly to Investors in Today's Market Money Managers Need to Recognize Poor Performance and Offer Fossil-Free Options*, Institute for Energy Economics and Financial Analysis, February 2019.

[10] *Who Owns the World's Fossil Fuels: A forensic look at the operators and shareholders of listed fossil fuel companies*, InfluenceMap, December 2018.

[11] *Who Owns the World's Fossil Fuels: A forensic look at the operators and shareholders of listed fossil fuel companies*, InfluenceMap, December 2018.

[12] Jamie Court, "Top 10 US Insurance Companies Invest $51 Billion In Fossil Fuels," Consumer Watchdog, 9 October 2018.

that fossil fuel companies could be forced to pay as climate change litigation makes progress in the courts.[13]

Lending to and 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 1.5ºC. Between 2016 and 2019, four American banks financed fossil fuels with more than $800 billion, which represented 30% of all global fossil fuel bank financing.[14] Banks will also suffer losses with mortgages, agricultural loans, and commercial real estate from increased frequency of fires, floods, and hurricanes.[15]

The Role of U.S. Financial Regulators

Climate change poses clear and serious risks to the financial system.[16] 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 a 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

- **Conduct real, meaningful climate risk oversight.** Banks and other financial institutions are reportedly using the COVID-19 crisis as an excuse to shirk common-sense climate risk responsibilities.[17] Regulators should incorporate climate risk into their prudential regulatory and supervisory framework.[18] That includes:
    - Mandating climate risk and impact disclosures and stress testing for financial institutions and the financial system as a whole, as well as issuing regulations to address and mitigate those risks;[19]
    - Lawmakers closing a glaring regulatory loophole by designating large asset managers and insurance companies as systemically important financial institutions (SIFIs); and
    - The Federal Reserve joining — as a full member — the Network of Central Banks and Supervisors for Greening the Financial System, an international network of central banks

[13] *The impact of climate change on the UK insurance sector: A Climate Change Adaptation Report by the Prudential Regulation Authority*, Bank of England Prudential Regulation Authority, September 2015; Jennifer Hijazi, "Climate liability is on the rise. Here's what it looks like," *E&E News*, 5 August 2019.

[14] *Banking on Climate Change: Fossil Fuel Finance Report 2019*, Rainforest Action Network, BankTrack, Indigenous Environmental Network, Oil Change International and the Sierra Club, 18 March 2020.

[15] Jennifer Hijazi, "Climate liability is on the rise. Here's what it looks like," *E&E News*, 5 August 2019.

[16] *Climate Change Threatens the Stability of the Financial System*, Gregg Gelzinis and Graham Steele, 21 November 2019.

[17] See, e.g., "Banks plead for rethink over post-crisis rules," *Financial Times*, 19 March 2020.

[18] See *Climate Change Threatens the Stability of the Financial System*, Gregg Gelzinis and Graham Steele, 21 November 2019, and *A Regulatory Green Light: How Dodd Frank Can Address Wall Street's Role in the Climate Crisis*, Graham Steele, January 2020.

[19] This could happen via regulatory action from agencies like the Federal Reserve. If the Fed doesn't act, Congress could pass legislation to require disclosures and stress testing, like the Climate Change Financial Risk Act of 2019.

and supervisors working together to address climate risk to national and global financial systems.

- **Ensure that banks can't own or trade fossils.** As fossil fuel companies crater, banks are reportedly maneuvering to take over assets from their most indebted clients outright.[20] Lawmakers should repeal the authority for banks to own physical assets like oil refineries, pipelines, tankers, power plants, and coal mines and trade commodities, or commodity companies that explore, drill, refine, transport, or export fossil fuels, specifically including such fossil fuels as crude oil, fracked gas, and coal.[21]

- **Invest in climate-resilient communities.** Lawmakers should establish a climate investment mandate to ensure that financial institutions with a federal charter invest a certain percentage of assets into climate change mitigation, resilience, and just transition efforts, with specific prioritization for communities and areas most impacted by environmental racism.

- **Integrate climate into fiduciary duty frameworks.** 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.

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[20] "Private Banks Owning Oil Companies is a Recipe for Disaster," Stop the Money Pipeline, 10 April 2020.
[21] The Protect Consumers from Market Manipulation Act would accomplish this. Under current statute, the Federal Reserve has authority to restrict this much more than it currently does, though to date it has not completed a pending rulemaking process to do so.