JOINT LETTER

Prevent a 'Climate Lehman Moment'

The collapse of Lehman Brothers triggered the last global financial crisis. There's a new threat on the horizon, yet a simple way to step back from the point of no return.

Brussels, 27 October 2021

To,

Neil Esho, Deputy Secretary General of the Basel Committee on Banking Supervision (BCBS)
Toshio Tsuiki, Deputy Secretary General of the BCBS
Pablo Hernández de Cos, Chairperson of the BCBS

The co-chairs of different BCBS groups, namely:

Task Force on Climate-related Financial Risks

Frank Elderson, European Central Bank
Kevin Stiroh, Federal Reserve Bank of New York

Risk and Vulnerabilities Assessment Group

Bertrand Rime, Swiss National Bank
Michael Gibson, Board of Governors of the Federal Reserve System

Supervisory Cooperation Group

Tomoko Amaya, Japanese Financial Services Agency
Ben Gully, Office of the Superintendent of Financial Institutions

Policy and Standards Group

Arthur Yuen, Hong Kong Monetary Authority
Korbinian Ibel, European Central Bank

Dear Basel Committee on Banking Supervision,

Right now, we run the risk of another financial crisis, this time caused by climate change. Climate scientists from around the world warn that global warming is dangerously close to being out of control.[1] There is global recognition that this crisis also threatens the stability of our financial system.[2] And yet, despite net-zero emission pledges, **most banks and insurers remain on a self-destructive path.[3] They perpetuate the risks of climate change by financing and insuring fossil fuel-related activities**.[4]

As the climate meltdown unfolds, financial institutions will face losses stemming from disruptive weather events, which intensify and increase in frequency. Examples abound, such as recent heavy flooding in Europe, a terrible instance of multi-billion dollar damages from catastrophic, climate change-related forces.[5] Such events are leading to huge unexpected payouts by insurance companies and to the destruction of assets and business operations that banks and insurers are exposed to. They cause unexpected market movements and asset price swings.

Furthermore, with the transition to a low-carbon economy, fossil fuel assets of banks and insurers will rapidly diminish in value or become entirely worthless. This will lead to massive losses for financial institutions, which could result in them requiring bailouts, where the public is the one to pay.

The truth is: we already have six times more fossil fuel reserves than we can afford to burn.[6] **Even the International Energy Agency (IEA) stated that if we want to meet the goals of the Paris Agreement, investments in new fossil fuels must stop immediately**.[7] This was recently echoed by United Nations Secretary-General Antonio Guterres.[8]

Therefore, any financing and insurance of new fossil fuel exploration and production is:

- **extremely risky, as new fossil fuels will lose their value.**
- **at odds with the Paris Agreement.**

An immediately feasible solution[9]

If a bank or insurer still wants to venture into an activity that explores and produces ***new fossil fuels***, they should be constrained to take the entire risk of funding this activity on their shoulders. Policymakers should introduce a **One-for-One rule for stability:** Every euro/dollar/pound etc. of financing provided must be matched by one euro/dollar/pound of institutions´ own funds, to be held liable. Their own funds should be sufficient to fully absorb losses without exposing depositors, policyholders and ultimately tax payers and society to the losses they will inevitably incur.[10]

Capital requirements for ***existing*** fossil fuel financing should also be increased, albeit to a lesser extent than that for new fossil fuels. This will allow the financing for existing fossil fuels to be phased out gradually, without jeopardising financial stability.

Such prudential regulation would:

- protect those who entrust their money with financial institutions, and prevent a potential financial crisis
- protect taxpayers, whose funds would otherwise be used in a bail-out scenario
- mitigate the risks of climate change in the first place, as the incentive in current prudential rules to finance fossil fuels, which equates to a subsidy, would be removed

Capital regulations for banks and insurers already mandate higher capital charges for high risk exposures. All we need to do is to make sure that fossil fuel exposures are recognised as high-risk within the existing rules.

This idea has been endorsed by a panel of 50 sustainable finance experts from across academia, civil society, commercial banks, central banks and the investor community.[11]

At the moment, financing and insuring coal, oil and gas projects remains artificially cheap. The capital levels that banks and insurers must maintain to cover potential future losses do not match the risks of these exposures. The lack of action so far is grounded in a paradox: Policy-makers and supervisors recognise the near impossibility of modelling climate-related risks due to the radical uncertainty of climate events.[12] But they say they need such modelling to be done before intervening. By waiting for these impossible calculations, **financial regulators extend an indirect subsidy to climate change-causing industries.**

We cannot wait. The climate clock is ticking. Other interventions on their own will not have the impact we need to prevent irreversible devastating impacts of climate change on the financial system.

As your leadership proves vital, we urge you to recognise the role of capital rules to avert a possible "Climate Lehman moment". This must-have request falls well in-line with the responsibility held by the Basel Committee on Banking Supervision (BCBS) to set international standards for banks.

Please conduct a systematic review of the entire Basil framework to make sure it addresses climate related risks. At the same time, coordinate with the International Association of Insurance Supervisors (IAIS), the standard setter for insurers. It is only with the highly impactful support of the BCBS that this pivotal proposal can be implemented in all jurisdictions.

Yours Sincerely,

111 organisations and **60** individuals, including civil society, ethical banks associations, economists and citizens (see full list below)

Annotations

1. IPCC (2021) *Climate Change 2021: The Physical Science Basis. Contribution of Working Group I to the Sixth Assessment Report of the Intergovernmental Panel on Climate Change*

2. See for example: Villeroy de Galhau, F. (2020) *The green swan*, Foreword; LAGARDE, C. (2020) *It is difficult to disagree that climate change is a threat to financial stability*; and CARNEY, M (2015) *Breaking the tragedy of the horizon – climate change and financial stability*.

3. Nagrawala et al (2021) *Countdown to COP26* and *Insuring Disaster*, ShareAction

4. The world's largest banks have *provided* $3.8 trillion to the fossil fuel industry since the Paris Agreement. For insurers, data *shows* that the largest U.S. and European insurers currently have invested around $600 billion in fossil fuels and the international insurance market for oil and gas totalled premiums of $17.3 billion in 2018.

5. Sheehan, M. (2021) *Europe floods largely uninsured, despite multi-billion industry loss: Aon*, Reinsurance News.

6. Carbon Tracker (2018) data *shows* that existing fossil fuel reserves amount to 2910 gigatonnes of carbon dioxide emissions, whereas the calculated carbon budget of our planet is 495 gigatonnes.

7. International Energy Agency (IEA) (2021) *Net Zero by 2050 - A Roadmap for the Global Energy Sector*, pg 222; *World Energy Outlook 2021*

8. Guterres, A (2021) *Secretary-General's statement on the IPCC report*

9. For banks: Philipponnat, T. (2020) *Breaking the climate-finance doom loop*, Finance Watch; For insurers: Norwood, P. (2021) *Insuring the Uninsurable*, Finance Watch

10. In terms of prudential rules, this means that banks and insurers should be required to finance activities related to new fossil fuel reserves entirely out of equity (own funds). Equity acts as a buffer that absorbs losses from banks´ and insurers´ financing activities.

11. Vaccaro, J. and Barmes, D. (2021) *Financial Stability in a Planetary Emergency*, Climate Safe Lending Network, Positive Money, in partnership with EIT - Climate KIC and the UN Environment Finance Initiative.

12. For example: Watts, J. (2021) *Climate scientists shocked by scale of floods in Germany*, The Guardian.

Finance Watch
Making finance serve society

Signatories of our joint letter:

111 organisations and **60** individuals, including civil society, ethical banks associations, economists and citizens

Organisations

1. Finance Watch
2. The Sunrise Project
3. Climate Safe Lending Network
4. Public Citizen
5. New Economics Foundation
6. Reclaim Finance
7. ClientEarth
8. 350.org
9. E3G
10. Positive Money UK
11. Transport & Environment
12. Insure Our Future
13. Bürgerbewegung Finanzwende
14. ShareAction
15. WWF European Policy Office
16. Cop26climateactionplan.Com
17. Change Finance
18. National Campaign for Sustainable Development Nepal
19. WEED - World Economy, Ecology & Development
20. Profundo
21. Fondazione Finanza Etica
22. ATTAC Liège
23. etika
24. Indigenous Peoples Global Forum for Sustainable Development, IPGFforSD
25. Clean Air Action Group
26. 350 Seattle
27. Connecticut Citizen Action Group (CCAG)
28. Fundacja Rozwój Tak – Odkrywki Nie
29. Re-set: platforma pro sociálně-ekologickou transformaci
30. ASUFIN
31. Climate Alliance Switzerland / Klima-Allianz Schweiz / Alliance climatique suisse
32. Revolving Door Project
33. Positive Money US
34. Majority Action
35. Sisters of St. Dominic of Caldwell, NJ
36. Sisters of Charity Federation
37. Ekumenická akademie (Ecumenical Academy)
38. BankTrack
39. Association of Ethical Shareholders Germany
40. As You Sow
41. KOTHOWAIN (Vulnerable Peoples Development Organisation)
42. Basel Institute of Commons and Economics
43. Rethinking Economics Australia

44. Fair Finance Institute
45. Debt Observatory in Globalisation (ODG)
46. Eerlijke Geldwijzer (Fair Finance Guide Netherlands)
47. Attac Togo (Lemou)
48. Attac Spain
49. Change Partnership
50. Freedom from Debt Campaign Pakistan
51. WEAll - the Wellbeing Economy Alliance
52. Association For Promotion Sustainable Development
53. Gestos (soropositividade, comunicação, gênero)
54. Fondation Nicolas Hulot
55. Attac Germany, Financial Markets & Tax Working Group
56. Rural Area Development Programme (RADP)
57. RIHRDO (Rural Infrastructure and Human Resource Development Organization)
58. Positive Money Europe
59. Global Policy Forum
60. Attac Austria
61. Institut Veblen pour les réformes économiques
62. Grands-parents pour le climat / Klima-Grosseltern CH
63. Galway One World Centre
64. Observatorio Mexicano de la Crisis
65. Financité
66. revo Prosperidad Sostenible
67. Waterkeeper Alliance
68. FracTracker Alliance
69. Polish Zero Waste Association
70. Both ENDS
71. Nipe Fagio
72. Finance Innovation Lab
73. NOVACT
74. Ban SUP (Single Use Plastics)
75. Servicios Ecumenicos para Reconciliacion y Reconstruccion Millersville University
76. Talousdemokratia – Economic Democracy Finland
77. Africa Europe Faith & Justice Network
78. European Federation of Ethical and Alternative Banks and Financiers
79. Fund Our Future
80. Lithuanian Consumers Alliance
81. Our New Economy
82. AfroLeadership
83. Jamaa Resource Initiatives
84. Iraqi Journalists Rights Defence Association
85. Institut Rousseau
86. Jovens para os Direitos Humanos Portugal / INCUB Portugal
87. Bio Vision Africa (BIVA)
88. Escape-jobs pour l'emploi sans carbone
89. Zukunftskonvent, Germany
90. The Gaia Foundation
91. Centre for Financial Accountability
92. Attac Norway
93. Development Alternatives with Women for a New Era (DAWN)
94. Global Justice Now
95. Fair Finance International
96. Agir pour le Climat
97. ZERO - Associação Sistema Terrestre Sustentável
98. European Trade Union Confederation
99. urgewald
100. Sustainable Value Investors
101. KoalaKollektiv
102. Leave it in the Ground Initiative (LINGO)
103. Global Peace and Development Organization
104. Les Amis de la Terre France / Friends of the Earth France
105. Fundación Finanzas Éticas
106. Campax
107. NOAH- Friends of the Earth Denmark
108. Rainforest Action Network
109. Global Alliance for Banking on Values
110. ZEF: Cooperative for ethical financing
111. Better Markets

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60. **Ysanne Choksey**, Citizen

… among a growing number of economists, influencers, citizens and campaigners who support us.