# **EBA Consultation on draft Guidelines on the management of ESG risks**

**EAPB comments**

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**General comments**

We welcome the opportunity to respond to the consultation paper on the draft guidelines on the management of ESG Risks. We welcome the overall nature of the guidelines and how they fit within EBA’s general objective of building an adequate framework to both (1) mitigate ESG risks and (2) support an orderly transition to a sustainable economy. It is in both of these purposes that the EAPB welcomes the opportunity to provide input at this early stage of regulatory proposal and implementation. With regards to the latter point made, the application date is dependent on application of the CRD, we would like to request the EBA to be clear but lenient in terms of application dates since timelines of consultations and papers are still ongoing and the CRR III is already coming into application January 2025. We assume that the CRD will apply from January 2026 but are asking the EBA to consider this in their overall roadmap.

We welcome, also, the following more specific, overall, aspects of the guidelines:

* The emphasis on the element of proportionality: the guidelines propose that the frequency and extent of materiality assessments is proportionate to the size and nature of the institution. The same applies to the extensiveness of the various risk management processes and procedures, which should be proportionate and specific to the outcomes of the institution’s materiality assessment;
* The initial emphasis on the “E”, with limited recommendations on “S” and “G”. Whereas we think it is relevant to expand the coverage of ESG risk management to including Social and Governance risks too, we welcome the qualitative nature of the proposals relating to them;
* The consistency efforts concerning other EBA guidelines, BCBS principles, EU Initiatives, CSRD/CSDDD legislations in terms of definitions.
* In terms of definition, we greatly welcome the EBA’s understanding that the assessment and management of ESG risks should take both impact dimensions into account to the extent that they affect the financial risks institutions are exposed to.
* The recognition that ESG risks are not an independent risk type, but a transversal risk driver in the sense that they influence traditional financial and non-financial risk types.

Overall suggestion relating to data:

We would like to suggest to EBA to reconsider the use of proxies throughout the proposals as stated in the guidelines (see Q6). The guidelines focus on internal procedures based on a structured collection of data. We experience that the collection of ESG data is still very challenging, with multiple issues ranging from comparability of data to coverage of data. For example, with public sector entities and SME’s excluded from CSRD requirements, some institutions like promotional banks are placed in a difficult position both in terms of data collection and reporting requirements.

Response to the EBA’s questions (part 7.2):

**Question 1. Do you have comments on the EBA’s understanding of the plans required by Article 76(2) of the CRD, including the definition provided in paragraph 17 and the articulation of these plans with other EU requirements in particular under CSRD and the draft CSDDD?**

We welcome the emphasis on CRD-based transition plans as focusing on the financial risk aspect of ESG and as risk management tools. It is important however that the tools used to meet the political goal of reaching climate neutrality by 2050 do not come in contradiction with the fundamental objectives of risk management. However, we would also welcome the possibility to set a single, coherent transition plan as an internal strategic document. This with the aim for institutions to proactively reflect on the changes driven by the sustainable transition, the risks and opportunities they entail, and prepare or adapt accordingly through structured transition planning. We believe that the approach of seeing “impact” and “risk” as two sides of the same coin is indeed conducive to this aim.

Also, we would like to request the EBA to elaborate on and investigate the potential tools (other than engagement with counterparties) that might be fit for mitigating risks and incorporating in the transition plan.

As for the articulation of the plans with other EU requirements, we would like to mention that CSRD is a reporting directive. It doesn’t require a setting of any transitional plan but just a disclosure in the case of existing or intended transitional plans. The EBA should ensure that its Guidelines are not contradictory to other legislative acts without overruling the scope of those frameworks.

**Question 2. Do you have comments on the proportionality approach taken by the EBA for these guidelines?**

We welcome considering proportionality principle by the EBA. The guidelines propose that the frequency and extent of materiality assessments is proportionate to the size of the institution. The same applies to the extensiveness of the various risk management processes and procedures, which should be proportionate and specific to the outcomes of the institution’s materiality assessment.

While we welcome the proportionality approach taken by the EBA for smaller institutions, we also think it shouldn’t stick to the definition of SNCI. The nature of the institution should be taken into consideration as well. Elements that could come into play are the homo- or heterogeneousness of the institution’s portfolio, the concentration of its assets, the different sectors the institution is active in, and elements related to the mandate of the institution – all of these are elements of great relevance to promotional banks. We do think the guidelines already provide an opening to this in the sense that the risk management processes are deemed to be proportionate to the actual risk materiality of the institution, of course based on a view or vision.

We also want to underline that the guidelines should clarify that for institutions that are dependent on an institution which is itself a significant institution, this daughter company should still benefit from proportionate requirements if it qualifies as an SNCI or meet the criteria suggested above.

**Question 3. Do you have comments on the approach taken by the EBA regarding the consideration of, respectively, climate, environmental, and social and governance risks? Based on your experience, do you see a need for further guidance on how to handle interactions between various types of risks (e. g., climate versus biodiversity, or E versus S and/or G) from a risk management perspective? If yes, please elaborate and provide suggestions.**

We welcome the approach taken by the EBA regarding the consideration of the different elements of ESG risks. The emphasis on the “E”, with minimum, and largely qualitative, requirements on “S” and “G” is something we deem appropriate for the time being.

This is only to say that institutions could make use of a more coherent view on how to incorporate social and governance risks in all of their risk identification, management, monitoring and mitigating processes. We would like to urge the EBA to provide more guidance or examples on this. But the same applies to even biodiversity and nature-related risks, which are already more challenging in terms of granularity of information and data, as compared to climate-related risks.

We would argue for a phase-in implementation of the guideines for aspects other than climate risks. Additional time is needed to cover social and governance topics, and some other environmental risks such as biodiversity. The data availability should be a prerequisite for further inclusion. The implementation timeline of other regulatory expectations such as the Corporate Sustainability Reporting Directive (CSRD) should be considered when tackling social and governance risks.

We greatly welcome the EBA’s understanding that the assessment and management of ESG risks should take both impact dimensions into account to the extent that they affect the financial risks institutions are exposed to. We encourage to take over the explanations in Par. 26 of background and rationale into the final text of the EBA GL.

**Question 4. Do you have comments on the materiality assessment to be performed by institutions?**

We would like to request the EBA to elaborate on the relationship between the materiality assessment as required under CSRD and the materiality assessment as required in the EBA guidelines, beyond the emphasis on consistency. We would also request the EBA to clarify the materiality assessment of non-EU exposures.

In paragraph 14 (c) "*most critical counterparties with regard to their deviations from the transition plans of their jurisdictions where they operate“* is too extensive for a bank-wide materiality analysis at portfolio level. The EBA needs to clarify the meaning of "most critical".

We would also like to request the EBA to specify expectations in terms of quantifying the materiality assessment and its outcomes. For some aspects there are no established calculation methods for quantifying, therefore qualitative assessment should be accepted where appropriate. Moreover, there should be a differentiated view on the time horizons only for the environmental perspective, but not for the S and G.

**Question 5. Do you agree with the specification of a minimum set of exposures to be considered as materiality exposed to environmental transition risk as per paragraphs 16 and 17, and with the reference to the EU taxonomy as a proxy for supporting justification of non-materiality? Do you think the guidelines should provide similar requirements for the materiality assessment of physical risks, social risks and governance risks? If yes, please elaborate and provide suggestions.**

We would welcome guidance on providing materiality assessment of not just physical risks, but also the qualitative assessment of social and governance risks. For all dimensions the guidance should be designed as recommendation, an example list and not as a minimum requirement. Therefore, we request EBA to delete the wording “at least” in Par. 14 as well as “and use” in Par. 14 lit. a). The implementation of the requirements in Par. 16 and 17 would be very granular, the regulatory need for the detailed justification should be reassessed as we suppose there would be many exemptions if classifying all listed sectors per se as materially subject to environmental transition risks.

**Question 6. Do you have comments on the data processes that institutions should have in place with regard to ESG risks?**

We would like to suggest to EBA to reconsider the use of proxies throughout the proposals as stated in the guidelines. The guidelines focus on internal procedures based on a structured collection of data. We would like to remind the EBA that the collection of ESG data is still very challenging, with multiple issues ranging from comparability of data to coverage of data. For example, with public sector entities and SME’s excluded from CSRD requirements, some institutions like promotional banks are placed in a difficult position both in terms of data collection and reporting requirements. For this reason, we argue that the data requirements specified in the Guidelines should be consistent with the data to be disclosed under the CSRD, including the timing of such requirements.

It would be welcomed if the EBA included considerations of the most important aspects of data needed to perform sound risk assessments, also including reflections of cost-efficiency of data collection for banks and customers. The inclusion of using sector data, as supported by the EBA Guidelines on Loan Origination and Monitoring, should also be considered. The same precision should be used in thinking of issues related to data quality, with for example the use of proxies. We would like to urge the EBA and ECB to make the aggregated information gathered through ECB stress testing and fit for 55 exercises available to the institutions.

Paragraph 25 (b) note that banks would be in charge of “data and methodologies used by data providers and performing regular quality assurance“, however we argue that banks should not be in charge of data quality insurance, since ESMA will handle the supervision of ESG rating providers.Using estimates as well as proxies should not be considered as an intermediate step. They could be a reasonable and meaningful instrument, especially in cases, where ESG-data will not be available in the foreseeable future, as is the case with granular SME exposures.

Please consider clarifying that Par. 23 is just a list to be considered as there could be data lack issues for some portfolios. Also, the phased-in implementation of CSRD should be taken into account.

Here we would like to repeat that CSRD is a reporting directive. It doesn’t require preparing any transitional plan but just a disclosure in the case of existing or intended transitional plans. Therefore, the wording in Par. 23 lit. a) ix) should be adjusted.

**Question 7. Do you have comments on the measurement and assessment principles?**

We welcome in general the approach envisaging a combination of exposure-, portfolio- and scenario-based methodologies. However, we would like to request the EBA for more flexibility in terms of which methodology should be used for different risk management processes.

Paragraph 22 should clarify that client engagement for data collection purposes may not be necessary especially if relevant data is available from public sources or disclosure under the CSRD. For some portfolios and/or exposure sizes, approaching all customers is neither feasible nor reasonable.

**Question 8. Do you have comments on the exposure-based methodology?**

The set of risk factors (Par. 31) should be designed as a list which should be considered (already indicated by “where applicable”, not as a minimum requirement, please delete “at least”. The likelihood estimation (lit. c) would remain especially complex and challenging in the near future.

**Question 9. Do you have comments on the portfolio alignment methodologies, including the reference to the IEA net zero scenario? Should the guidelines provide further details on the specific scenarios and/or climate portfolio alignment methodologies that institutions should use? If yes, please elaborate and provide suggestions.**

The proportionality approach should apply in this context too. Institutions should be left the freedom to discern which (material) portfolios should be focused on in their assessments on alignment to net-zero targets. The methodologies should also be consistent with Pillar 3 alignment templates.

**Question 10. Do you have comments on the ESG risks management principles?**

Again, we welcome the recognition that ESG risks are not an independent risk type, but transversal in the sense that they influence traditional financial and non-financial risk types.

Again, we would like to request the EBA to provide more guidance in terms of the examples of risk management tools to optional consider in managing ESG risks. Par. 42 refers to 10 year time horizon which is challenging, and should be designed as a recommendation list with points which should be considered, not as a minimum requirement.

**Question 11. Do you have comments on section 5.2 – consideration of ESG risks in strategies and business models?**

Par. 43 should be designed as a recommendation list with points which should be considered, not as a minimum requirement.

**Question 12. Do you have comments on section 5.3 – consideration of ESG risks in risk appetite?**

The separate consideration of ESG as a risk driver when defining the bank’s risk appetite is questionable, as it affects the traditional risks. More flexibility in defining risk appetite is needed. A higher level of granularity than at country level may be too small-scale for large institutions with diversified business models.

**Question 13. Do you have comments on section 5.4 – consideration of ESG risks in internal culture, capabilities and controls?**

We would like to request the EBA to ensure consistency with the EBA Guidelines on Internal Governance and the concept of the three lines of defence, in terms of the internal culture, capabilities, controls and governance appropriate for ESG risk management.

**Question 14. Do you have comments on section 5.5 – consideration of ESG risks in ICAAP and ILAAP?**

We welcome the overall requirement of incorporate environmental risk in ICAAP based on adverse, forward-looking scenarios. However, we would like to emphasize that the ICAAP specifically is an internal process and here again the principle of proportionality should be implemented: it is the responsibility of the institution to implement this in a proportionate matter that reflects the materiality of the risks it is exposed to.

The most frequent time horizon in the ICAAP is 3 years. A multi-year calculation going beyond this should not be mandatory. The longer-term time horizon should only serve to inform the normative and economic perspective with regard to ESG risk drivers.

**Question 15. Do you have comments on section 5.6 – consideration of ESG risks in credit risk policies and procedures?**

Using qualitative methods should be allowed.

**Question 16. Do you have comments on section 5.7 – consideration of ESG risks in policies and procedures for market, liquidity and funding, operational, reputational and concentration risks?**

There is no need in special requirements on concentration risk in this Guideline.

**Question 17. Do you have comments on section 5.8 – monitoring of ESG risks?**

We agree with the proposals of monitoring ESG risks through effective internal reporting frameworks and through early warning indicators and thresholds. We would like the EBA to consider that such indicators and thresholds are best set at a sector or portfolio level, for the aim of monitoring ESG risk in the portfolio of the institution, rather than at an individual client or entity level. In our view, key risk indicators are a great tool for this In addition, in paragraph 70, the term "most significant portfolio" should be further defined.

**Question 18. Do you have comments on the key principles set by the guidelines for plans in accordance with Article 76(2) of the CRD?**

Whereas we appreciate the principle of consistency, we do not believe that each element of the transition plan should be aligned to the process of materiality assessment as the plan should first and foremost be a strategic approach or internal document elaborating on the institution’s view and business strategy for rendering the transition possible and how it will face the risks and opportunities entailed by this transition.

We would welcome the possibility to set a single, coherent transition plan as an internal strategic document. We would like to mention that CSRD is a reporting directive. It doesn’t require a setting of any transitional plan but just a disclosure in the case of existing or intended transitional plans. The EBA should ensure that its Guidelines are not contradictory to other legislative acts without overruling the scope of those frameworks.

**Question 19. Do you have comments on section 6.2 – governance of plans required by the CRD?**

We are concerned about the requirements included in this principle regarding the first Line of Defence (business) responsibility for concluding whether counterparties’ transition plans are credible and sound. We believe it should be the responsibility of public institutions to put in place effective measures to assess and monitor the credibility and soundness of the counterparties’ transition plans, and also think engagement with all of an institution’s counterparties is unreasonable and unfeasible.

We would also like to suggest removal of the reference to the compliance function from par. 86 b) as the risk limits referred to in this paragraph are typically monitored by the risk management function.

**Question 20. Do you have comments on the metrics and targets to be used by institutions as part of the plans required by the CRD? Do you have suggestions for other alternative or additional metrics?**

No comments.

**Question 21. Do you have comments on the climate and environmental scenarios and pathways that institutions should define and select as part of the plans required by the CRD?**

No comments.

**Question 22. Do you have comments on section 6.5 – transition planning?**

**Question 23. Do you think the guidelines have the right level of granularity for the plans required by the CRD? In particular, do you think the guidelines should provide more detailed requirements?**

**Question 24. Do you think the guidelines should provide a common format for the plans required by the CRD? What structure and tool, e. g., template, outline, or other, should be considered for such common format? What key aspects should be considered to ensure interoperability with other (e. g., CSRD) requirements?**

For questions 22 to 24: Again, we welcome the emphasis on CRD-based transition plans as focusing on the financial risk aspect of ESG and as risk management tools. However, we would also welcome the possibility to set a single, coherent transition plan as an internal strategic document. This with the aim for institutions to proactively reflect on the changes driven by the sustainable transition, the risks and opportunities they entail, and prepare or adapt accordingly through structured transition planning. We believe that the approach of seeing “impact” and “risk” as two sides of the same coin is indeed conducive to this aim. Several comments raised throughout this response to the guidelines, for example related to limitations in terms of data collection or risk management tools, are applicable here as well.

As mentioned above, CSRD is a reporting directive. It doesn’t require preparing a transition plan, but disclosing information if it is existing or intended. The EBA should give more flexibility on transition plans at this stage, gather information from the coming CSRD reports and evaluate them on risk aspects to be considered in the future regulation.

**Question 25. Where applicable and if not covered in your previous answers, please describe the main challenges you identify for the implementation of these guidelines, and what changes or clarifications would help you to implement them.**

No comments.

**Question 26. Do you have other comments on the draft guidelines?**

No comments.