

CFTC Report: Effectively Meeting the Challenge of Climate Change

Climate change poses a major risk to the stability of the U.S. financial system and to its ability to sustain the American economy . . . A major concern for regulators is what we don't know. This is the message of a report titled *Managing Climate Risk in The U.S. Financial System*, published by the U.S. Commodity Futures Trading Commission, September 9, 2020 ([here](#)). The report was prepared by the Climate-Related Market Risk Subcommittee, Market Risk Advisory Committee of the CFTC.

The first of its kind report for the agency, concludes that climate change is already impacting, or is anticipated to impact, nearly every aspect of the economy and human health unless steps are immediately taken. The risks include “disorderly price adjustments in various asset classes . . . as well as potential disruption” of the proper functioning of financial markets. Those risks are so significant that simply dealing with them may prove so disruptive that the process will itself “pose risks to the financial system if markets and market participants prove unable to adopt to the rapid changes. . .” required. This is because to mitigate those risks the economy must be transitioned to “net-zero” emissions.

Much is known about the risks of climate change, the Report notes. Regulators need to move forward using that information to help provide solutions. At the same time, much is not known about unfolding risks. For example, while “understanding about particular kinds of climate risk is advancing quickly, understanding about how different types of climate risk could interact remains in an incipient stage. Physical and transition risks may well unfold in parallel, compounding the challenge.” Those unfolding risks may also spawn others from existing frailties and weaknesses in systems. It is thus critical that calls to strengthen and support regulators be headed.

Equally critical to properly handling existing risks and those that will unfold will be close coordination between the public and private sectors. The Report thus calls for regulators to work “closely with the private sector to ensure that financial institutions and market participants . . .” are effectively working together to address the risks, adopt current

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systems and innovate new ones to effectively move forward. The solutions to the risks being faced will no doubt require “new financial products, services and technologies . . .”

The Report concludes with a series of recommendations, bolstered by detailed citations, which include the following:

- Financial markets will only be able to channel resources efficiently to activities that reduce greenhouse gas emission if an economy-wide price on carbon is in place at a level that reflects the true social cost of those emissions
- Climate change could pose systemic risks to the U.S. financial system
- Regulators should be concerned about risks of climate-related “sub-systemic” shocks, that is those that impact a particular sector, asset class or region of the country
- Existing legislation provides U.S. financial regulators with wide-ranging and flexible authorities that could be used to start addressing financial climate-related risk now
- Regulators and market participants around the world are generally in the early stages of understanding and experimenting with how best to monitor and manage climate risk
- Insufficient data and tools to measure and manage climate related financial risks remain a key constraint
- The disclosure by corporations of information on material climate related financial risks is essential, although the existing disclosure regime has not resulted in sufficient information to be useful to market participants and regulators
- International engagement by the U.S. could be significantly more robust

The lengthy, thoughtful report, represents not just a map for addressing climate change but for moving the economy forward in a positive manner.