



Climate Change and U.S. Financial Regulators: Overview and Recent Actions

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Under the Biden Administration, financial regulators have announced a range of new measures to address financial risks associated with climate change. The Department of the Treasury, the Securities and Exchange Commission (SEC), and the Federal Reserve have each announced new steps:

- The Treasury’s announcement covers a range of issues including public spending, macroeconomic effects, and international cooperation.
- The SEC’s addresses investor disclosure requirements relating to climate risks and the classification of funds marketed to investors as environmentally friendly.
- The Fed’s relates to lending risks for individual financial institutions and to systemic financial risks related to climate change.

This Insight provides an overview of these actions and how they interrelate.

Background: Financial Sector Climate Risks

An international standard-setting body, the Financial Stability Board, [has noted](#) that climate change can affect financial stability and asset prices either through [physical risks](#) such as more damaging storms and wildfires or through [transition risks](#) in which changes in government policies or market perceptions might lead to sudden asset price changes. [By some estimates](#), assets held by fossil fuel companies globally could drop between \$250 billion and \$1.2 trillion or become “stranded assets” in a possible transition away from fossil fuels.

Estimates of potential losses to the financial sector from physical risks are relatively large. In the housing market, [one paper found that](#), as of 2019, government-sponsored enterprises [Fannie Mae and Freddie Mac](#) guaranteed \$6.88 trillion in home mortgage debt without pricing flood risk into their guarantee fees. Almost all insured U.S. flood risk is backstopped by the U.S. government through the [National Flood Insurance Program](#).

There is evidence that investors are already seeking to price climate risks into asset prices. In the roughly \$4 trillion U.S. municipal bond market, [one paper concluded](#) that counties more likely to be affected by

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climate change paid more in underwriting fees and initial bond yields when issuing long-term municipal bonds.

Recent Actions

Treasury

On January 27, 2021, the [White House issued an executive order](#) promising to expand financing internationally for projects to reduce GHG emissions or promote climate adaptation, and on April 22, 2021, [released](#) its International Climate Finance Plan focused on ways to mobilize public and private funds internationally toward climate-friendly goals. That plan [involves the Department of the Treasury](#) working with other U.S. government agencies and multilateral development banks to manage climate-related risks internationally. In a [July 11, 2021, speech](#), Secretary Janet Yellen noted the United States would double by 2024 its annual public climate finance for developing countries to about \$5.7 billion per year and triple its public finance for climate adaptation to about \$1.5 billion.

In an [April 21, 2021, speech](#), Yellen detailed how Treasury would look at international cooperation, tax, and macroeconomic policy issues to promote climate goals and stressed the importance of making climate risk disclosures more standardized and clearer. This would enable investors to compare risks across companies and drive capital toward cleaner energy, Yellen noted. Clearer climate disclosures—the purview of regulators such as the SEC—could impact GHG emissions targets [if investors demand higher returns for climate risk](#). Some argue, however, that [assessing](#) “actionable” [climate risks for investors](#) can be challenging or misguided. [Others argue](#) disclosures alone may prove insufficient to mitigate systemic risks.

Yellen [announced](#) April 19, 2021, the creation of a “climate hub” within Treasury to coordinate three areas: (1) climate transition finance, (2) climate-related economic and tax policy, and (3) climate-related financial risks.

Securities and Exchange Commission

SEC Chair Gary Gensler in a [July 28, 2021, speech](#) said he had requested the SEC’s staff develop a mandatory climate risk disclosure rule proposal for the commission’s consideration by the end of 2021 to update the [agency’s 2010 guidance](#). Gensler noted that such mandatory disclosures should be “consistent and comparable,” enabling investors to compare both qualitative and quantitative metrics across companies, including those related to GHG emissions, financial impacts of climate change, and progress toward climate-related goals. In February 2021, [Allison Herren Lee, then acting SEC chair, directed the SEC’s Division of Corporation Finance](#) to enhance its focus on climate-related disclosure in public company filings.

The SEC also [announced in March 2021](#) the creation of a “Climate and ESG [Environmental, Social, and Governance] Task Force” within the SEC’s Division of Enforcement to identify misconduct related to funds branded as ESG. In recent years, funds marketed to investors as “ESG” have grown markedly, but there is [no universally agreed-upon](#) or legally binding definition of what constitutes an ESG fund. In April 2021, [the SEC’s Division of Examinations warned](#) that a review it conducted of ESG funds found a number of misleading statements regarding ESG investing processes and adherence to voluntary global ESG frameworks.

Federal Reserve

On January 25, 2021, the Fed announced the creation of an internal Supervision Climate Committee to strengthen its “capacity to identify and assess financial risks from climate change” and “develop an appropriate program to ensure the resilience of supervised firms to climate-related financial risks.” In a March 2021 speech, Fed Governor Lael Brainard announced the creation of a Financial Stability Climate Committee at the Fed to assess and address climate-related risks to financial stability.

Fed Vice Chair for Supervision Randall Quarles spoke about the Financial Stability Board’s publication of a roadmap for addressing international climate-related financial risks in a July 2021 speech. The FSB roadmap supports coordination of climate disclosures for standard-setting bodies internationally. The Fed announced in December 2020 it had formally joined the Network for Greening the Financial System, a group of over 80 central banks focused on climate-related risks that has begun developing methodologies for conducting climate stress testing. Also, the Fed is co-chairing the Basel Committee on Banking Supervision’s Task Force on Climate-Related Financial Risks.

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