Your response has been received by EBA

Dear user,

Thank you very much for your interest in the European Banking Authority (EBA) and for submitting your comments to one of our consultations. Your response has been received and will be taken into account by the EBA. Please find below, for your records, the response you have submitted.

Please note that this email address is not monitored and does not accept replies. If there is something wrong or missing in your response to the consultation, please contact us at *info@eba.europa.eu*.

Kind regards,

European Banking Authority

Your answers are:

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?

In order to clarify our following positions, we would like to emphasize that these developments of the EBA's mandate are to be considered through a broader prism than prudential regulation. Indeed, as a key European institution, the EBA should contribute to the European Union's pursuit of climate neutrality (see the EU 2050 long-term strategy) and, in particular, to its endeavour to align finance flows (see Art.2.c of the Paris Agreement, UNFCCC 2015). The EBA should maintain in focus that its extended mandate incorporates micro-prudential supervision in line with the EU collective effort on climate finance.

The inclusion of environmental, social and governance (ESG) issues within the prudential risk framework is particularly important. Notably considering, on the one hand, the considerable risks of build-ups of climate and environmental (C&E) -related financial risks throughout the banking and financial system, and on the other, the crucial role of banks for the transition to a low-carbon economy. Moreover, transition plans' contribution to an enhanced ESG risk management is key in providing a forward-looking approach. The latter appears to be particularly important to capture risks over the medium and long term, beyond the traditional horizon of banking and disclosure practices.

The EBA's uptake of these issues, in accordance with Article 87a(5) of Directive 2013/36/EU, and the adjustments made to CRR and CRD articles are as such welcomed. This mandate should nonetheless be apprehended outside of the current siloed approach to ensure no misalignment with other European institutions' endeavours is introduced, notably referring to initiatives of the European Commission, so it contributes to building a robust framework for climate finance. Regarding transition plans, we believe the EBA's added value, rather than redefining their content and process, should rather be on how the transition plans, as specified in CSRD and CSDDD, should inform the risk management framework.

It is paramount to consider there should be a unique transition plan. Convergence towards a single definition and framework should then be a priority for EU institutions, which should avoid contributing to confusion and reporting burden.

The AEFR Working Group on Transition Plans (abbreviated below by AEFR WGTP) considers the EBA, throughout these guidelines, introduces a confusion with the specific notion of 'prudential transition plans' and the underlying problematics. From this perspective, we note the EBA does not properly follow its mandate to spur the integration of ESG considerations in banking practices, through developments in the prudential framework, and in particular to articulate its approach with the other EU requirements, namely CSRD and CSDDD.

As we explain in our second recommendation to unlock transition plans' potential (AEFR, n°5/2023), "transparency and comparability cannot be achieved if every transition plan which is disclosed if based on divergent definition, structure, or information. In the absence of a common framework, transition plans users would naturally tailor their requests for information according to their anticipated use. This inevitably results in an unnecessary burden for the organisation and inefficiencies." We then continue with the proposal to reconciliate transition plans' uniqueness with their multiple usage, calling "for the definition of common core pillars that would be complemented by additional key building blocks associated with a particular usage. The key pillars would ensure there exist a unique transition plan framework (that includes common definitions, structure, and core information), while addressing specific requirements of the different users with additional blocks that will expand some sections of the transition plan. For instance, in the case of a [banking] institution, prudential supervision would require the organisation to undertake detailed analysis regarding the evolution of its portfolio(s) [' risk] under various stress scenarios. However, the detailed information would not need to be included in a transition plan addressed to the general public (the relevant information for the latter would rather be on the [bank]'s portfolio decarbonisation path and the result of alternative scenarios)."

We thus consider the narrative that the prudential approach justifies a separate plan (see section 3.3. of the guidelines, and in particular §13 and 17) is both erroneous and prejudicial for the plans' role in the transition, while being detrimental to the credibility of the transition plan for banks' stakeholders.

At the very core of the EBA's approach to transition plans, we furthermore find a confusion on transition plans' diverse usages. As we detail in Section 3.4. (AEFR, n°5/2023), there exist several reasons prompting an organisation to plan and disclose its transition; risk management is one of them amongst strategy, external communication/disclosure and regulatory compliance/supervision. The AEFR WGTP first notes the EBA's guidelines use the distinction between the "(prudential) risk" and "business model" (i.e., strategy) approaches to justify the constitution of a distinct 'prudential plan'. This cannot hold considering (i) the need for a unique transition plan as previously stated, (ii) the significant overlap of risk-management and strategy-based approaches to the transition. It is impossible for a credit institution to develop two different plans, which might result in specific orthogonal actions such as credit granting and portfolio allocation. Furthermore, the EBA's guidelines fail to segregate these intertwined approaches; section 5.2 (§44.a) explicitly refers to portfolio alignment as part of strategies and business models, and section 6.1 (§77) to strategic KPIs within (prudential) risk-based plans. Such a mix contributes to demonstrate these two usages cannot justify distinct exercises.

Finally, the AEFR WGTP welcomes the attention of the EBA to articulate its guidelines with the existing EU requirements and in particular those under CSRD and the CS3D, but highlights these guidelines fail to do so. In particular, we consider "the elaboration of plans under CRD" should be considered in a building blocks approach and as such cannot "support institutions in addressing other requirements, such as CSDDD requirements and CSRD disclosure requirements on business strategies and transition plans" (section 3.3. §14). On the contrary, 'CRD plans' would only complement the CSRD/CS3D plans with building blocks on prudential-specific requirements, which would not need to be disclosed. We also develop, for Question 20 of this consultation, on inconsistencies between the EBA's CRD and CSRD plans.

As we have expressed in our seventh recommendation (AEFR, n°5/2023), the current silo organisation of EU institutions should be overcome to streamline strategic approaches: "[s]upervisory and regulatory entities should overcome mandate discrepancies to avoid diverging strategic and risk approaches to the transition. This would help clarify the stakeholders' environment (e.g., limiting standard multiplicity) and would allow for efficiency (e.g., limiting compliance burden, policy alignment, etc.).

Moreover, the framework for transition plan and transition planning "should be constructed on existing requirements and build on the well advanced European regulatory framework". In the light of defining a unique framework for transition plans, we call for CSRD/ESRS requirements to be considered as the baseline for all EU initiatives on transition plans, while we encourage EFRAG to provide a definition of transition plan and planning pillars, accompanied by technical guidelines and standards. (Recommendations 2 and 3, AEFR n°5/2023). Additional information may be added within complementary building blocks, if deemed needed to achieve the CRD mandate. Any overlap with existing disclosure requirements on strategy, business models, risk management, and metrics should be carefully eliminated.

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.
The approach taken by EBA should follow the CSRD/ESRS disclosure requirements and associated definitions, across the whole ESG framework.

Overall, as we detail in Section 5.4 (AEFR, n°5 2023): "The transition characteristics of a bank portfolio should be explicitly affirmed as a mitigant to climate transition risk over the medium and long term. Indeed, as climate risks materialises over time mainly through credit risk, the lower the proportion of stranded assets, the less the vulnerability of the portfolio to climate risks. This implies that the transition characteristics of a bank portfolio should be considered in the SREP as part as the business model analysis, as well as in the climate-related scenario analysis, which is consistent with a dynamic balance-sheet approach. Individual transition plans will also be a key input to financial institutions' counterparty risk management assessment. It however requires financial institutions to handle thousands of counterparties in a consistent manner. While this can be facilitated by a unified transition planning framework it would also require further standardisation and specification of relevant transition target and performance metrics per sector (and in particular calculation of scope 3 emissions, relevant categories for scope 3 target or value chain definition, etc.).”

Furthermore, we recommend (see Recommendation 11, AEFR n°5/2023) the scope of transition plans and transition planning are promptly extended to include other environmental and social issues than climate mitigation. Also, we call the EBA to consider, in addition to CSRD/ESRS requirement, the NGFS’ holistic approach to Nature related risks, which encapsulates Climate risk into the broader Environmental risks, rather than adopt a siloed approach of each Environmental goal.

Question 4: Do you have comments on the materiality assessment to be performed by institutions?
The materiality assessment should be consistent with the materiality assessment process defined in CSRD/ESRS. In particular, time horizons should be the same.

Question 6: Do you have comments on the data processes that institutions should have in place with regard to ESG risks?
While we agree on the fact that “[i]nstitutions’ internal procedures should provide for gathering information needed to assess the current and forward-looking ESG risk profile of counterparties, by aiming at collecting client and asset-level data” (Section 4.2.1. §23), we note an inconsistency in the proposed guidelines. On the one hand, the EBA’s guidelines reference EU reporting rules (“Directive 2013/34/EU” and “Directive 2022/2464”) and insist on ‘articulating CRD and CSRD plans’. On the other hand, the definition of metrics to be disclosed as per Section 4.2.1. presents divergences from information disclosed under CSRD/ESRS. Note that as it stands, client and asset-level non-financial information will be made available in the EU by disclosures made under CSRD/ESRS requirements. The AEFR WGTP underlines that such a misalignment between metric requirements under CSRD/ESRS and the one defined in these guidelines bets on the illusory and burdensome consideration that banking organisations adopt this additional set of disclosure requirements and fill the gaps by collecting more information throughout their value chain. (E.g., “collecting non-public data from counterparties on their sustainability profile [and determining] for which other counterparties they require the

submission of their transition plans as part of business relationships". Section 6.5., §102).

Note, such a bank-specific 'questionnaire' approach is extremely cumbersome, not only for the banks, but also for the businesses, which would be exposed to multiple requests from their banking partners. The CSRD has set up an extensive reporting framework for ESG data that is quite unique at international level, attempting to calibrate the reporting burden of companies and the need for ESG data.

In line with our call for a CSRD-based transition plan backbone with additional building blocks, the AEFR WGTP considers the EBA's guidelines should only reference CSRD/ESRS metrics with complementary prudential-specific ones. Such complementary data should be added only if deemed useful and material for measuring and managing ESG risks.

We furthermore note inconsistencies on metrics definition within the guidelines. For instance, disclosure guidelines on GHG scope 1-2-3 emissions are both "in absolute and/or intensity" (Section 4.2.1 §23.a.ii.) and in absolute terms (Section 6.3.ii, §94.a). A CSRD explicit reference would avoid creating additional inconsistencies. We also note these ESRS-specific requirements may pose some implementation challenges for some corporates, but creating additional and divergent requirements on data will only be burdensome and hamper their use.

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.
Please refer to answer to Question 21 for comments on scenarios.

Question 11: Do you have comments on section 5.2 – consideration of ESG risks in strategies and business models?
This is covered in CSRD/ESRS and needs to be fully aligned.

Question 12: Do you have comments on section 5.3 – consideration of ESG risks in risk appetite?
This is covered in CSRD/ESRS and needs to be fully aligned.

Question 13: Do you have comments on section 5.4 – consideration of ESG risks in internal culture, capabilities and controls?
This is covered in CSRD/ESRS and needs to be fully aligned.

Question 17: Do you have comments on section 5.8 – monitoring of ESG risks?
This is covered in CSRD/ESRS and needs to be fully aligned.

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?
In order to ensure "consistency of prudential plans with other processes and communications", the AEFR WGTP recommends that time horizons are clearly stated within the key principles section and that the dedicated section explicitly refers to CSRD requirements. The possible articulation with ECB guidelines could also be included to guarantee interoperability. We thus call for amending Section 6.3.i. §92 so it details CSRD time horizons (less than one year, between one and five years, more than five years, and other requirements).

Question 19: Do you have comments on section 6.2 – governance of plans required by the CRD?
The AEFR WGTP agrees on the importance of governance and accountability for transition plans, notably through the allocation of responsibilities across LODs and throughout the organisation.

We furthermore consider transition planning, in particular, should ensure ownership and accountability at the highest level. "The quality of the transition planning process must be a key topic that a board should assess, to get comfort on the capacity of the company to engage in a credible transition pathway. The incorporation of the elements of the transition planning process, as a complement to the transition plan itself, in the management report (URD in the EU) solidifies the ownership and accountability of the board. The board also needs to ensure, for the company's strategy at large, that the policies and procedures are in place to foster the implementation of the transition plan. Additionally, the board needs to monitor closely the progress in implementation and the outcomes." (Section 4.2.2., AEFR, n°5/2023).

Nonetheless, we consider the guidelines should reference CSDDD and CSRD requirements rather than proposing a less detailed and ambitious guidance on the management's body's responsibility for approval and oversee. In order not to fragment the EU approach for the governance of ESG-related risks, we call for the EBA not to provide additional guidance on CSDDD and CSRD requirements.

In addition to the issue of regulatory fragmentation, we note the guidelines are evasive on the implementation of monitoring. For instance, no precise timeline is defined; the management body should be "regularly informed of relevant developments and progress achieved in relation to the institution's targets." (Section 6.2.i. §85).

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?
Considering the unique plan with building blocks approach we call for (Reco. 2, AEFR, n°5/2023), metrics and targets should be clearly defined as per the ESRS (CSRD) with potential additional datapoints to fulfil specific requirements of the prudential risk approach. Note some of these additional datapoints are likely to be identified in the upcoming ESRS sector-specific disclosure requirements for banks, which would therefore necessitate a complete alignment is ensured.

Moreover, we note that, in addition to lacking consistency with CSRD/ESRS requirements, the guidelines relating to metrics and targets for the 'CRD plan' remain vague. The AEFR WGTP underlines here the importance of precise and prescriptive requirements that are essential to ensuring robustness and comparability of transition plans. We consider such prescriptive requirements are defined by the ESRS. For instance, we find very few details on what "quantifiable targets" stands for and implies. Also, some other vague definitions might be pointed out, such as the guideline on "setting targets and milestones at regular time intervals", in comparison to ESRS prescriptions.

These elements are to be read in conjunction with what we have detailed in answer to Question 6 regarding data misalignment implications and in Question 18 on time horizons.

Also, we wish to highlight possible difficulties from banking institutions to harvest granular entity-level data, in particular per legal entity, that require the use of Group-level proxies.

Furthermore, we may underline that, while banks are expected to play a key role for the accelerated adoption of robust and transparent transition plans throughout the economy–notably with an extended engagement with their clients– it should be recalled that such market forces are not sufficient to guarantee data and transition plans' quality. The EBA guidelines should therefore remain clear on the role of banks on the matter and consider the parallel need to organise an efficient external assessment (please refer to Section 4.2.6., AEFR, n°5/2023).

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?

Scenarios and pathways definition are indeed key issues that guidelines on transition plan and planning should identify. In Section 3.3.i. (AEFR n°5/2023), we note "discrepancies regarding the target state of the economy, and specifically regarding the use of reference scenarios."

"Reference scenarios may first be used in the construction of the stakeholder's scenario to define baseline assumptions and targets. Considering industry specificities, reference scenarios may also identify decarbonisation levers, their priority in use (by order of importance and/or ease of operationalisation) and the required timeframe. Stakeholders might then tailor this insight to their own business specificities. A second use is to serve as a benchmark reference for the stakeholder's assumptions. For instance, the stakeholder might justify its use of Carbon Capture, Utilisation and Storage (CCUS) with the argument that it is aligned with assumptions considered in a reference scenario. It is important though to keep in mind that reference scenarios provide a general view of what the economy/sector could look like in terms of total GHG emissions, technology use, investment trend, etc. This general view may therefore be challenged." (Reco. 8, AEFR, n°5/2023)

The EBA's guidelines rightfully identifies institutions should consider science-based and publicly available scenarios. We also note the guidelines mention examples of reference scenarios (i.e., form the IEA and the EU JRCG), to which we propose to add scenarios from the IPCC and NGFS, being already recognised and used by numerous banking organisations. We provide further details on the latter in Figure 3 and Annex 5.i (AEFR, n°5/2023).

In addition, we identify limitations in the use of reference scenarios and ways to improve their quality in the light of transition planning (Reco. 8, AEFR, n°5/2023). The EBA's guidelines on scenarios could investigate these limitations and adapt its guidance to consider associated (prudential) risks.

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

The AEFR WGTP welcomes the fact the EBA considers the importance of transition planning. We discuss this crucial matter in Section 4. (AEFR, n°5/2023).

However, we expect that EFRAG provide detailed guidance on transition planning, specifically on assumptions, execution and monitoring (reco. 4, AEFR, n°5/2023). We furthermore detail that "the credibility of the transition plan will be dependent on the credibility of the transition planning. From a practical standpoint, the forward-looking nature of transition planning requires choices to be made about key assumptions, shaping the stakeholder's vision of the future low-carbon economy. Nevertheless, we observe the current economic environment fails to provide clear guidance on several key notions, which implies stakeholders may adopt divergent positions when building their scenarios. To ensure transition plans are credible and efficient for the transition towards a low-carbon economy, we consider it is crucial to follow a robust approach on the selection of assumptions, and to provide transparency on key assumptions, as well as on their update and monitoring. We provide an example of the broad categories that could be included in transition planning guidelines and their articulation with the CSRD disclosure requirements".

The EBA's guideline for institutions to "clearly lay out the internal processes by which they prepare for a transition to a more sustainable economy and implement their objectives and targets i.e., transition planning process, […]" (Section 6.5., §101) is then insufficient.

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?

Please refer to answers to other questions.

Overall, let us state again that the EBA's guidelines should be seen as a complement to CSRD plans and provide additional granularity, if relevant, to define the prudential building block complementing the unique plan.

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?
Please refer to answer to Question 1 where we explain why the EBA should not provide any format/structure/tool/template/… that does not correspond to the specific case of defining an additional building block (if deemed relevant) to complement CSRD plans with a prudential risk approach.

The key aspect to consider in order to ensure interoperability is to avoid fragmenting the EU transition plan landscape by creating an additional definition a transition plan framework. The best interoperability is to construct on existing elements (reco. 3, AEFR, n°5/2023).

Question 26: Do you have other comments on the draft guidelines?
In the light of the general approach presented by the EBA throughout these guidelines, we would like to underline the limitations of the transparency/disclosure approach for the inclusion of ESG considerations within banking operations. In particular, we note section 3.3. §14 and §15 (already mentioned in Question 18).

On section 3.3. §14, we also wonder how the EBA conciliates its guidelines that on the one hand explain not requiring "to set out an objective of fully aligning with Member States or Union sustainability objectives or one specific transition trajectory" (i.e., a 1.5°C or NZE objective), and on the other hand the requirements on portfolio alignment (6.3.ii §94.b).

Also, we seek for more information from the EBA's guidelines regarding the assessment of "the robustness of [transition] plans as part of the supervisory review and evaluation process" (Section 3.2 §6.4).

The AEFR WGTP would furthermore like to react on section 7.1.D "Options considered". We call for options to be reconsidered in the light of our previous comments and so it guarantees alignment with CSRD/ESRS requirements rather than acting divergences.

To conclude, the AEFR WGTP cordially invites the EBA to consider the attached AEFR Debate Paper “Transition plans: ensuring their comparability, credibility and effectiveness to accelerate the low carbon transition” (n°5/2023) in which we identify and discuss key issues for unlocking transition plans and planning for the transition.

Upload files
transition_plans_ensuring_their_comparability_credibility_and_effectiveness_to_accelerate_the_low_carbon_transition.pdf (1.01 MB)

Name of the organization
Assocation Europe-Finances-Regulations (AEFR) - Working Group on Transition Plans

© European Banking Authority - **https://www.eba.europa.eu**