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Statement by
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Subcommittee on Financial Institutions and Monetary Policy

Climate-related Financial Risk

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Good morning, Chairman Barr, Ranking Member Foster, and members of the subcommittee; thank you for inviting the National Credit Union Administration (NCUA) to discuss the agency's activities regarding climate-related financial risk. My name is Rendell Jones, and I am the Deputy Executive Director for the NCUA.

As a regulator and insurer, the NCUA is responsible for examining and supervising for credit union resilience against all material risks. As the NCUA's 2022–2026 Strategic Plan notes, credit unions should consider how climate-related financial risks may affect their membership and institutional financial performance. The agency's current work in this area aims to enhance its understanding of these risks.

The agency believes credit unions are best positioned to assess various risks and opportunities within their specific fields of membership. Climate change presents several conceptual and practical challenges for credit unions and the NCUA. Just as credit unions must continue to adapt to account for climate-related financial risks, among other risks, the NCUA must evolve its understanding of the impact on credit unions, credit union members, the credit union system, and the National Credit Union Share Insurance Fund (Share Insurance Fund).

In my testimony, I will summarize NCUA's climate-related financial risk activities, including the recent voluntary request for information (RFI) from stakeholders, and reiterate the agency's legislative priorities.

Climate-related Activities

Interagency Involvement

The NCUA is engaged in interagency efforts to study and address climate-related financial risks. On May 21, 2021, the Financial Stability Oversight Council (FSOC), of which the NCUA is a voting member, was asked to assess climate-related financial risks, both physical and transition risks, concerning the stability of the financial system.[1] To complete this task, the FSOC established a Climate-related Financial Risk (CFRC) committee composed of its members. The NCUA participates in the FSOC's CFRC and its working groups. In addition, the FSOC CFRC has formed a Climate-related Financial Risk Advisory Committee, which helps the FSOC gather information on climate-related financial risks from various stakeholders, including the credit union industry.

Through the FSOC's CFRC, NCUA staff participate in discussions, provide regulatory expertise, and review and contribute to the CFRC's report to the FSOC. NCUA staff are also working with other FSOC member agencies to test a data and analytics platform developed by the Office of Financial Research for FSOC CFRC members to facilitate analysis of climate-related financial risks and collaboration on research.

Research Note

As part of the agency's efforts, the NCUA published a research note summarizing estimates of credit union exposure to climate-related physical risks in April. The NCUA's Office of the Chief

[1] Executive Order on Climate-Related Financial Risk, May 20, 2021; https://www.whitehouse.gov/briefing-room/presidential-actions/2021/05/20/executive-order-on-climate-related-financial-risk/.

Economist paired credit union call report data with the Federal Emergency Management Agency's (FEMA) National Risk Index, which measures a community's vulnerability to the adverse effects of 18 natural hazards.[2] The NCUA's analysis showed that roughly one-quarter of federally insured credit unions, accounting for one-third of system-wide assets, are headquartered in communities particularly vulnerable to natural disasters, including hurricanes, floods, drought, and wildfires. The research also showed that minority depository institutions are at even greater risk, with more than half located in communities at relatively high or very high risk of experiencing adverse effects from natural hazards.

The credit unions most at risk of negative outcomes due to natural hazards tend to be located in coastal areas, particularly in California, Texas, and Florida. These three states account for 11 percent of credit unions located in communities with an elevated risk and 22 percent of credit union assets. Further, the research examined the exposure of the credit union system to specific natural disaster risks, focusing on the ten most costly natural disasters based on FEMA's estimates of expected annual losses. Roughly half of the credit union system's assets are in areas at a relatively high or very high risk of experiencing a natural disaster due to a tornado, and a similarly large share of credit union assets are in areas exposed to strong winds.

Floods, droughts, hurricanes, and other climate-related events damage or destroy homes, farms, small businesses, vehicles, and vital infrastructure. This damage has a cost, including to federally insured credit unions that finance house purchases, vehicles, and member small business projects. Therefore, the NCUA should analyze all potential material risks to credit union performance and develop tools or resources to help credit unions measure, monitor, and mitigate climate-related financial risks.

Request for Information
In late April, the NCUA issued a voluntary request for information (RFI) seeking input from stakeholders and subject matter experts to strengthen the agency's ability to identify and assess credit unions' current and future climate-related financial and natural disaster risks.

The NCUA's goals in issuing the RFI are twofold. First, the agency seeks to improve its understanding of climate-related financial risks, how credit unions view them, and how it can best support the industry in mitigating them. And second, the agency aims to better understand the products and services credit unions can offer to leverage opportunities presented by any related transitions in the economy's energy, transportation, construction, housing, and other applicable sectors.

In the NCUA's RFI, the agency requested voluntary feedback and included 38 questions for the public's consideration. It solicited input on a variety of topics, including:

- Climate-related physical and transition risks that are affecting or may affect the industry in the future;

[2] Estimating Credit Union Exposure to Climate-Related Physical Risks, National Credit Union Administration, Office of the Chief Economist, Published on April 19, 2023. Available at https://ncua.gov/news/publication-search/climate-financial-risk/estimating-credit-union-exposure-climate-related-physical-risks.

- Potential adjustments to operations, governance, and business strategies to mitigate those risks, and methods, metrics, and tools for identifying and measuring those risks; and
- Climate-related business opportunities, including the support needed to expand products and services and any barriers that credit unions might face.

The comment period closed on June 26, 2023, and the agency received 44 responses from individual credit unions, credit union trade associations, and other interested parties. These and other insights provided by stakeholders and our fellow federal and state regulators will be essential in shaping future efforts by the NCUA to identify and assess climate-related risks to federally insured credit unions, develop tools to assist credit unions in managing those risks, and produce guidance and support programs to help credit unions safely leverage any related member service opportunities.

As noted in the RFI, the NCUA does not plan to use the information collected in the examination and supervision of individual credit unions. Any new requirements for credit unions associated with climate-related financial risk would require changes to examination and supervision procedures and approval by the NCUA Board before implementation.

Legislative Priorities

By measuring, monitoring, and mitigating risks, including climate-related financial risks, the NCUA can fulfill its statutory mandate of maintaining the safety and soundness of credit unions, protecting consumers, and safeguarding the Share Insurance Fund. Statutory modifications to the Federal Credit Union Act (the Act) could bolster the agency's efforts.

For example, the NCUA Board has requested a statutory change allowing the agency's Central Liquidity Facility program to permit corporate credit unions to purchase capital stock on behalf of a subset of their members. The CLF addresses short-term liquidity needs, like those created from weather-related events, which cause community-wide disruptions.

In addition, the NCUA, unlike other federal banking regulators, does not have the statutory authority to examine and supervise third-party vendors. With more credit union operations moving to parties outside the NCUA's purview, the agency cannot accurately assess all potential risks to the system and the Share Insurance Fund. Closing these gaps in our nation's financial regulatory structure will help the NCUA mitigate risks to the Fund and protect the credit union system and credit union members from unexpected events more effectively.

Finally, because the 2008 financial crisis demonstrated that significant failures or other shocks to the system could quickly deplete the Share Insurance Fund's equity levels, the NCUA seeks to remove the statutory limits on the normal operating level, so the Board can more proactively manage the Fund. This change would give the NCUA more flexibility to assess premiums to build, over time, enough equity in the Share Insurance Fund to manage significant insurance events, including climate-related financial risks, without impairing credit unions' contributed capital deposits. These recommended changes are consistent with the FDIC's Deposit Insurance Fund operations.

The NCUA appreciates the subcommittee's continued support of the NCUA and acknowledges Ranking Member Foster's work to enact legislation that would close regulatory blind spots the NCUA continues to face.

Conclusion

The credit union system remains well-capitalized, stable, and well-positioned to handle various economic possibilities. The NCUA continues to monitor for any material risks to credit union performance and the health and stability of the Share Insurance Fund.

Thank you for the invitation to testify before you today. I look forward to answering your questions.