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### ◆ INTRODUCTION

The potential impact of climate change is an emerging risk insurers should proactively assess and monitor. Record global catastrophes in recent years illustrate the implications of climate change on weather-related losses and the potential for it to extend to all aspects of business. Last year, a number of large-scale U.S. weather events pushed global insured losses to \$77 billion, according to Swiss Re.<sup>1</sup> This followed record global insured losses in 2011 of \$126 billion.

The issue of climate change is complex, but there is growing evidence severe weather events are occurring with greater frequency and severity than previously predicted. Given these trends, it is important for insurers to identify climate-related factors and evaluate how they will impact their business and the exposures they indemnify. Recognizing the need to ensure insurers account for any potential effect these risks might have on the marketplace and the availability and affordability of insurance, state insurance regulators and other stakeholders have moved forward to administer a climate risk disclosure tool. This article outlines some of these efforts.

### ◆ MULTI-STATE ADMINISTRATION OF THE INSURER CLIMATE RISK DISCLOSURE SURVEY

In 2012, the insurance departments of California, Washington and New York administered the *Insurer Climate Risk Disclosure Survey* (survey) for the 2011 reporting year as part of a multi-state initiative. The survey was required for insurers writing more than \$300 million in direct premium in these states, covering 85% of the U.S. insurer market. The multi-state initiative was designed to bolster participation in the survey by capturing most of the insurance industry. Approximately 470 company responses were collected in 2012 and made publicly available on the California Department of Insurance's website.<sup>2</sup> It should be noted uniform responses were permitted for insurers that are part of a group.

The multi-state initiative was expanded this year when the insurance departments of Connecticut and Minnesota announced they would also require the survey. Additionally, the required reporting threshold was lowered from \$300 million to \$100 million in direct written premium and applied mandatorily to all individual companies writing business in one of these states, regardless of where they are domiciled. Assuming full reporting compliance, the new \$100 million premium threshold is expected to double the number of reporting companies to more than 1,000 in 2013.<sup>3</sup> This should give insurance regulators, investors and policyholders a better picture of how insurers are responding to climate change.

The California Department of Insurance, which serves as the central filing point and data warehouse, now offers companies the ability to submit their data directly online. The move to online filing will allow submitted data to feed directly into a database that is sortable by regulators and interested parties, enabling more people to provide analysis. It is anticipated survey questions will remain consistent with the 2010 adopted version in the short-term to create a benchmark of responses, enabling response changes to be more easily observed.<sup>4</sup>

### ◆ A CLOSER LOOK AT THE NAIC INSURER CLIMATE RISK DISCLOSURE SURVEY

The *Insurer Climate Risk Disclosure Survey*, adopted by the NAIC in 2010, was designed to be an insurer reporting mechanism that would provide regulators with a window into how insurers' assess and manage risks related to climate change. The eight-question survey asks insurers to provide a description of how they incorporate climate risks into their mitigation, risk-management and investment plans. They are also asked to identify steps taken to engage key constituencies and policyholders on the topic of climate change. A full text of all questions is available on the California Department of Insurance website.<sup>5</sup>

The survey was modeled after the CDP (formerly named the Carbon Disclosure Project) voluntary questionnaire and, as such, cross-references its questions. The CDP questionnaire asks respondents to disclose their greenhouse gas emissions, water management and climate change strategies. Although the CDP holds the largest collection of self-reported climate change data, insurer participation is low. Insurance regulators developed the NAIC survey as a way to fill the void of pertinent climate risk information. Insurers typically disclose such things as their carbon footprint reduction efforts, modeling, physical risk assessments, liability concerns, investment strategies and underwriting policies. Many also report on climate change-related innovations and green practices, such as sustainable real estate, catastrophe bonds, renewable energy practices and green reconstruction.<sup>6</sup>

Ceres recently released (March 2013) a report, *Insurer Climate Risk Disclosure Survey: 2012 Findings and Recommendations*, which analyzed the 2012 survey results from California, New York and Washington. Not surprisingly, the re-

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<sup>1</sup> "Swiss Re: U.S. Dominates 2012 Insured Cat Losses." (2013, March 27).

<sup>2</sup> NAIC. Dec. 1, 2012, Climate Change and Global Warming (E) Working Group. [Working Group Minutes]

<sup>3</sup> NAIC. Aug. 8, 2013, Impact of Climate Disclosure Survey (E) Subgroup. [Subgroup Minutes]

<sup>4</sup> Ibid.

<sup>5</sup> [www.insurance.ca.gov/0250-insurers/0300-insurers/0100-applications/financial-filing-notices-forms/annualnotices/ClimateSurvey.cfm](http://www.insurance.ca.gov/0250-insurers/0300-insurers/0100-applications/financial-filing-notices-forms/annualnotices/ClimateSurvey.cfm).

<sup>6</sup> Ibid.

port found cost efficiencies and weather-related loss reductions served as the driving force behind insurers implementing climate change strategies.<sup>7</sup> The report also noted property/casualty insurers were most engaged in mitigating the impact climate change can have on weather-related losses. Loss reduction strategies most commonly cited included limiting geographical and investment catastrophic exposure, expanding exclusions and defensive underwriting. Alternatively, life insurers' climate risk mitigation activities were found to center on their investments, with nearly a quarter of life insurers indicating they actively manage climate change risks on invested assets.

### ◆ 2013 FINANCIAL CONDITION EXAMINERS HANDBOOK REVISIONS

In 2012, state insurance regulators, working through the NAIC, adopted revisions to the 2013 *Financial Condition Examiners Handbook*. These updates provide examiners with needed guidance on what questions to ask insurers regarding any potential impact of climate change on solvency. The questions were specifically designed to help examiners identify unmitigated risks and to provide a framework for them when examining such risks and their impact on how an insurer invests its assets and prices its products. The updates made changes to the handbook's Exhibit B – Examination Planning Questionnaire, Glossary, Interview of Investment Management, Interview of Chief Risk Officer, Exhibit V – Prospective Risk Assessment, Investment Repository and Underwriting Repository sections.<sup>8</sup>

### ◆ OTHER INSURER-RELATED CLIMATE CHANGE DISCLOSURE INITIATIVES

#### SEC Disclosure

Effective Feb. 8, 2010, the U.S. Securities and Exchange Commission (SEC) adopted guidelines designed to assist public companies in incorporating climate change information into the SEC's existing disclosures. According to the SEC, the guidance was in response to several petitions for interpretive advice submitted by large institutional investors and other investor groups. The SEC's guidance specifies that companies note any regulatory, legislative, operational, and financial impact from climate change. Specific disclosure areas within an SEC filing that a company should consider include: Impact of Legislation, Regulation Impact of International Accords, Indirect Consequences of Regulation or Business Trends, and Physical Impacts of Climate Change.<sup>9</sup>

#### CDP Disclosure Questionnaire

The CDP, based out of the United Kingdom, is a not-for-profit organization formed to promote climate sustainability initiatives for businesses, governments and cities. The organization provides a framework for the largest collection

of self-reported climate change data from corporations, governments and cities worldwide.<sup>10</sup> Much of this data is collected through an annual questionnaire that asks respondents to disclose their greenhouse gas emissions, water management and climate change strategies. The CDP initiated its first annual data request in 2003, with only 221 companies responding.<sup>11</sup> It currently has more than 4,000 organizations participating in the disclosure questionnaire.<sup>12</sup>

Each year, the CDP requests climate-related data from the 500 largest global organizations, referred to as the Global 500. The *CDP Global 500 Climate Change Report 2013* provides an analysis of how respondents are addressing the impact of climate change on their businesses. It includes an examination of sector trends based on 404 (81%) of the top 500 corporations participating in the questionnaire.<sup>13</sup> Among the largest 50 carbon emitters, the report found carbon emissions were growing, with overall emissions remaining substantially unchanged over the past five years.

As emissions are closely tied to economic activity, businesses will need to change their business models to prevent emissions from rising as the economy recovers. The report also highlighted a lack of reporting on carbon emissions in several business activity areas. Additionally, the report found financial incentives were the primary driving force behind corporate climate change actions. This suggests financial incentives established by regulators would be a powerful impetus for change. Regulation and physical risks were the most commonly cited risks by companies in the report. Identified opportunities were less quantifiable, but included changing consumer behavior and reputation.

#### United Nations Environment Programme Financial Initiative Survey

The United Nations Environment Programme Financial Initiative (UNEP FI) is a partnership between the United Nations Environment Programme (UNEP)—the United Nations systems designated entity for addressing environmental issues at the global and regional levels—and the financial sector. The UNEP FI works with more than 200 global and diverse

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<sup>7</sup> Ibid.

<sup>8</sup> NAIC. Dec. 1, 2012. Climate Change and Global Warming (E) Working Group. [Working Group Minutes]

<sup>9</sup> U.S. Securities and Exchange Commission, SEC: Commission Guidance Regarding Disclosure Related to Climate Change. [Release Nos. 33-9106; 34-61469; FR-82]. February 2, 2010.

<sup>10</sup> CDP [Home Page]. Retrieved Sept. 20, 2013. Retrieved from [www.cdproject.net/en-US/Pages/HomePage.aspx](http://www.cdproject.net/en-US/Pages/HomePage.aspx).

<sup>11</sup> Newell, Andrea. "What is the Carbon Disclosure Project?" *TriplePundit*. November 2010.

<sup>12</sup> "Are you new to CDP?" Carbon Disclosure Project. Retrieved Sept. 20, 2013, from [www.cdproject.net/faqs.asp](http://www.cdproject.net/faqs.asp).

<sup>13</sup> CDP. (2013). "Global 500 Climate Change Report 2013."

## CLIMATE CHANGE RISK DISCLOSURE INITIATIVES (CONTINUED)

types of insurers and investment firms. The goal of the UNEP FI is to better understand how environmental, social and governmental (ESG) issues impact financial and economic performance. In keeping with this goal, the UNEP FI issued the agenda-setting *Insuring for Sustainability* report in 2007, which outlined good practices in sustainable insurance strategies, products and services.<sup>14</sup>

In 2008, the UNEP FI collaborated with Temple University's Fox School of Business to produce the first global survey on ESG factors related to insurance underwriting and product development. The survey, *Advancing the Role of the Insurance Industry in Climate Change Adaptation*, is a voluntary comprehensive online survey with results provided in an aggregate format. The survey aims to: 1) identify climate-related risk-management and risk-transfer activities, products and services of the insurance industry and major changes in these areas; and 2) assess how the insurance industry can support countries by facilitating increased resilience to climate-related risks. The survey results, published in *The Global State of Sustainable Insurance* report, highlighted ESG issues are influencing underwriting decisions with varying influence across lines of business. The results also indicated there is a gap between policy and regulation frameworks and how these issues manifest themselves as risk to insurers.<sup>15</sup>

In response to these survey results, the UNEP FI decided to implement the Principles for Sustainable Insurance (PSI) Initiative, a principles-based global framework to assist insurers in better managing ESG risks. The PSI Initiative is a U.N.-backed, insurer-led approach to drive the adoption and implementation of voluntary and aspirational global principles and actions to manage risk and opportunities related to ESG issues. Once a company commits to these disclosures, they are asked to publicly and annually disclose progress on their signatory-determined aspirations and targets for each principle. The purpose of the disclosures is to demonstrate accountability and transparency to all stakeholders on implemented progress.<sup>16</sup>

### Global Reporting Initiative

Based in Amsterdam, the Global Reporting Initiative (GRI) is a global network of approximately 30,000 people and functions as the Collaborating Centre of the UNEP. The GRI provides a global Sustainability Reporting Framework of disclosures, guidelines and sector supplements. It publishes sustainability reports intended to provide consistent, transparent and comparable data.<sup>17</sup> Its *Sustainability Reporting Guidelines* include disclosure on broad areas, including economic, environmental and social performance. In June of this year, the GRI and CDP signed a memorandum of understanding, agreeing to align their reporting frameworks.<sup>18</sup> The result should assist in creating more integrated frame-

work of sustainability reporting and guidelines for companies to follow when reporting their sustainability efforts.

### ◆ CONCLUSION

Disclosure of climate risk is important because of the potential impact climate change can have on insurer solvency and the availability and affordability of insurance across all major categories. Munich Re estimates weather-related losses increased nearly fourfold in the U.S. since 1980. In that time, insurers faced losses of \$510 billion from extreme weather events such as prolonged droughts, hurricanes, floods and severe storms. Experts predict climate change will continue to intensify the frequency and severity of these types of weather-related events. This poses the potential for increased pressure on solvency, not only from physical insured losses, but also from losses on invested assets, insured lives and degraded health standards. Additionally, insurers must navigate legal uncertainty and regulatory changes related to climate change. Adaptation will require insurers to incorporate these changing dynamics into their risk-management schemes, corporate strategies and investment plans.

The need for disclosure increases as the risk of climate change becomes more apparent and quantifiable. Without disclosures, regulators, investors and other stakeholders would be unable to assess how insurers are addressing climate-related risks. Disclosures also benefit insurers, providing them with a benchmark from which to assess their own climate change strategies and strengthening their ability to identify how climate change impacts their business. Furthermore, disclosure allows policymakers to gain an insight into needed public policy changes.

### ABOUT THE AUTHOR

Anne Obersteadt is a researcher with the Center for Insurance Policy and Research (CIPR). She has more than 13 years of experience with the NAIC performing financial, statistical and research analysis on all insurance sectors. Prior to the NAIC, she worked as a commercial loan officer at U.S. Bank. Obersteadt has a bachelor's degree in business administration and an MBA in finance. She also studied abroad at the University of Guadalajara.

<sup>14</sup> NAIC. March 6, 2012. Climate Change and Global Warming (E) Working Group. [Working Group Minutes]

<sup>15</sup> Ibid.

<sup>16</sup> Ibid.

<sup>17</sup> "What is GRI?" Global Reporting Initiative. [www.globalreporting.org](http://www.globalreporting.org).

<sup>18</sup> Companies to benefit as CDP and GRI collaborate to harmonize reporting frameworks. Global Reporting Initiative. Retrieved Sept. 20, 2013, from [www.globalreporting.org/information/news-and-press-center/Pages/Companies-to-benefit-as-CDP-and-GRI-collaborate-to-harmonize-reporting-frameworks.aspx](http://www.globalreporting.org/information/news-and-press-center/Pages/Companies-to-benefit-as-CDP-and-GRI-collaborate-to-harmonize-reporting-frameworks.aspx).

<sup>19</sup> Munich Re Press Release. "North America most affected by increase in weather-related natural catastrophes." October 2012.



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