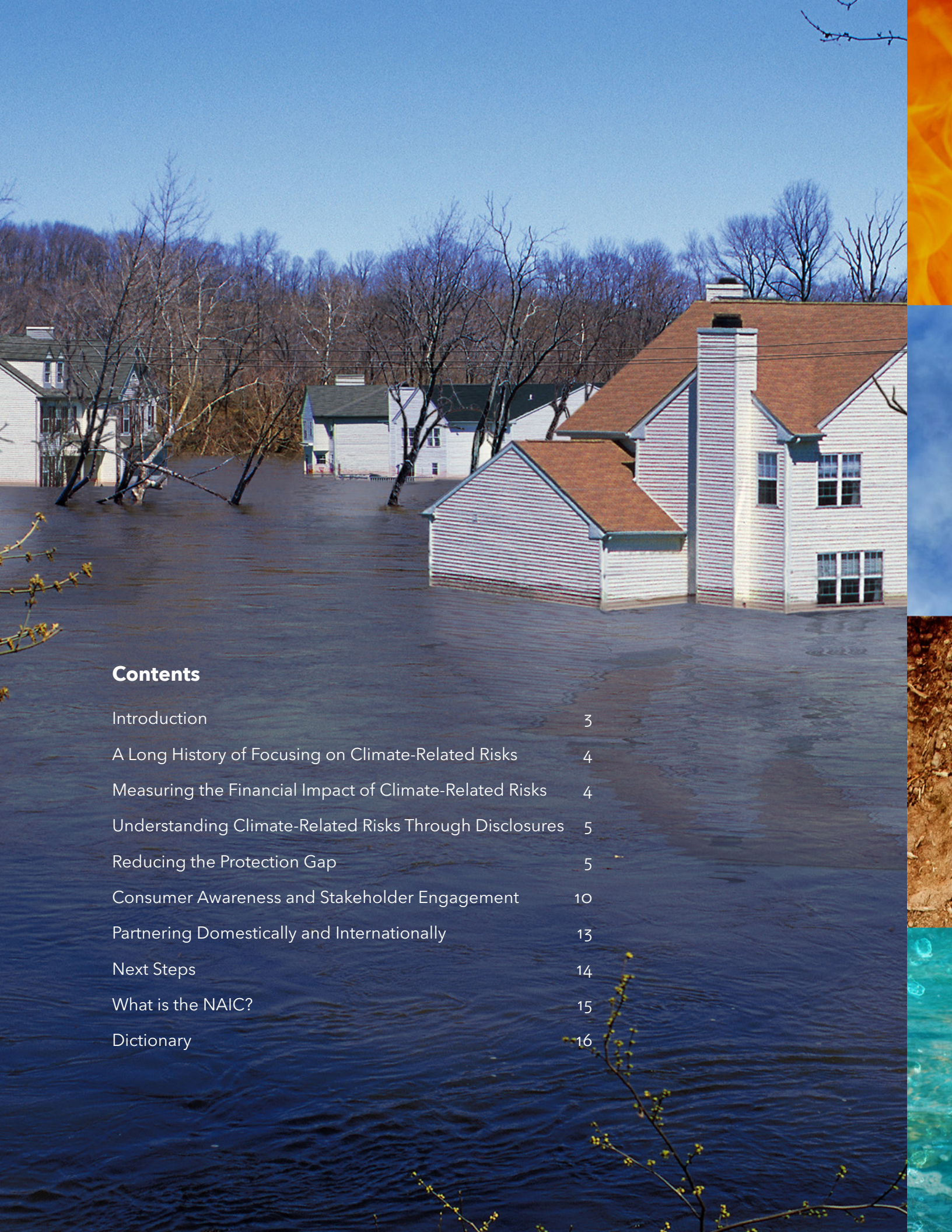


Adaptable to Emerging Risks

The State-Based Insurance Regulatory System is Focused on Climate-Related Risk and Resiliency



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The role of state insurance regulators in managing climate-related risks is critical.





Oregon Insurance Commissioner Andrew R. Stolfi, Washington Insurance Commissioner Mike Kreidler, and then-Utah Insurance Commissioner Todd E. Kiser discuss insurance issues facing homeowners and local governments in the wake of the Camp Fire with California Insurance Commissioner Ricardo Lara.

State insurance regulators are on the front lines of climate-related natural catastrophe preparedness and response, protecting policyholders and maintaining well-functioning insurance markets.

The NAIC, which brings together state insurance regulators, has long been committed to monitoring and addressing how climate-related risks affect policyholders and the insurance industry.

There's critical work being done in every state, and it's an issue that continues to change rapidly. Our insurance regulatory system is accustomed to adapting to an evolving risk landscape and is well-positioned to address the challenges presented by climate-related risks both today and in the future.

For more than 150 years, from the first fire insurance policies influencing building codes to today's record-breaking natural catastrophes driving population shifts, state insurance regulators have experience and insight into the impact of climate-related risk on insurance and consumers.

Since the NAIC's first meeting in New York in 1871, when discussions on storms and the evolving science around weather were a part of the agenda, we've understood how climate-related risks need to be monitored and managed.

Our focus has been in three key areas:

- Financial risk analysis.
- The availability and affordability of insurance.
- Risk awareness and mitigation.



State insurance regulators listen to a presentation on climate-related risks.

A Long History of Focusing on Climate-Related Risks

The NAIC and state insurance regulators have been working to address weather-related risks for more than a century. During the first NAIC meeting, state insurance regulators discussed how the modern-day innovative communication device, the transatlantic telegraph, could facilitate a better understanding of weather-related information. Since then, the NAIC has worked to provide its membership with data, expertise, and resources to help state insurance regulators address the economic impact of natural disasters.

In 2008, the NAIC began a modernization initiative to perform a critical assessment of the insurance solvency regulation framework, which put state insurance regulators in a better position to regulate current and prospective risks faced by the insurance industry, including climate-related risk. This initiative put state insurance regulators in a better position to effectively identify company exposures, determine vulnerabilities, and collaborate to resolve concerns related to solvency.

Measuring the Financial Impact of Climate-Related Risks

State insurance regulators—as risk management specialists—are aware of the challenges that climate-related risk may pose to the insurance sector.

Insurers may be exposed to climate-related risk on both sides of their balance sheet:

1. On the asset side through their investments.
2. On the liability side based on the types of policies they underwrite.

The NAIC collects financial data from more than 4,500 insurers, representing more than 98% of U.S. premiums. The data is used for financial analysis, including risk-based capital (RBC) and other solvency-related reviews. The financial data includes information on insurer investments, which can be used to assess industry investment exposure to various risks.

The NAIC's Capital Markets Bureau monitors and analyzes developments and trends in the financial markets for state insurance regulators, including tracking and monitoring investment exposures. In 2021, the NAIC contributed to an International Association of Insurance Supervisors (IAIS) study assessing the potential quantitative impact of climate-related risk on insurers' investments.

In 2017, to recognize increased exposure to catastrophic events, the RBC formula was expanded to include a specific charge for hurricane and earthquake risks.

Understanding Climate-Related Risks Through Disclosures

More than a decade ago, the NAIC adopted the Insurer Climate Risk Disclosure Survey to identify trends, vulnerabilities, and best practices for managing climate-related risk. The survey covers key topics, including climate risk governance, risk management, modeling and analytics, stakeholder engagement, and greenhouse gas management. As of 2021, 15 states participated in the survey, representing nearly 80% of the market by direct written premium.

State insurance regulators are currently considering revising the survey to align with the Financial Stability Board's (FSB's) Task Force on Climate-related Financial Disclosures (TCFD). This alignment will strengthen the supervisory tool, improve consistency across sectors and jurisdictions, and help identify practices to be shared for continuous improvement.

Reducing the Protection Gap

State insurance regulators work to ensure that premiums are not excessive, inadequate, or unfairly discriminatory while balancing that insurers have enough money to pay claims. The key to maintaining this balance is a competitive insurance market. The NAIC supports state insurance regulators in managing their markets by offering tools and shared resources, including:

- Collecting data and information, including premiums and losses, claims, and consumer complaints.
- Developing best practices for encouraging growth in private flood insurance.



More than a decade ago, we created our first committee focused on climate-related risk and resiliency issues.



Connecticut Insurance Commissioner Andrew N. Mais works with the Red Cross to assess damage.

- Conducting applied research to explore the economic benefit of increasing resilience to wildfire.
- Identifying innovative insurance products designed to fill coverage gaps.
- Exploring the benefits of mitigation and resilience to reduce losses before natural hazards occur.

State insurance regulators need access to data and information to assess the health of their markets. This assessment is done on an ongoing basis and is used to make critical decisions that protect consumers. The NAIC supports states in their efforts by collecting data and information that can be used to monitor their markets and understand how insurance prices and coverage options are evolving over time.

While the majority of flood coverage is still purchased through the National Flood Insurance Program (NFIP), state insurance regulators have been advocating for growth in the private flood insurance market to provide consumers with more choices. In 2019, the NAIC adopted a report to identify ways for state insurance departments to encourage that growth. In addition, the NAIC developed a requirement for insurers to include a line item highlighting private flood activity in their annual financial statements. Through the Market Conduct Annual Statement (MCAS), the NAIC also collects information on exposures, claims, lawsuits, and complaints about private flood insurance.



State insurance regulators meet to discuss mitigation programs.

A proposal to create a Catastrophe Model Center of Excellence (COE) within the NAIC's Center for Insurance Policy and Research (CIPR) has been developed. If it's adopted, it will provide resources for state insurance regulators, including access to CAT modeling documentation, technical education and training, and applied research to proactively address regulatory climate-related risk and resilience priorities.

Innovative insurance products can also play a role in reducing the protection gap. Insurers have an opportunity to create new products and adapt the way claims are paid. The NAIC has provided forums to discuss ways that innovation can address climate-related risk and close protection gaps.

A critical component to closing the protection gap is reducing the risk before disasters strike. The NAIC has highlighted state mitigation programs and economic incentives for improving community resilience. For example, its CIPR conducted a study in partnership with the Insurance Institute for Business & Home Safety (IBHS) and Risk Management Solutions (RMS) exploring the economic benefits of wildfire resilience strategies in nine communities through California, Colorado, and Oregon.

The NAIC hosted a building code, mitigation, and resiliency funding workshop in 2021 to educate stakeholders about the building code update and approval process, state mitigation actions, and funding options for community resilience. The NAIC compiled a list of actions policyholders can take to reduce the risk of property loss. The information also included discounts required by state law and programs designed to help justify cost reductions for insureds.



(left) NAIC staff and state insurance regulators review the damage from hail as part of an IBHS symposium.

(below) IBHS demonstrates how better building materials can reduce risks from wildfire.



NAIC: ADAPTABLE TO EMERGING RISKS



JOIN US
ON JUNE 18 AT 2 PM ET
FOR A TWITTER CHAT ON
FLOOD RISK
AND PREPARATION

#YOURRISKISREAL

Social media post from the NAIC's disaster preparedness campaign.

Consumer Awareness and Stakeholder Engagement

NAIC worked with insurance departments across the country to launch an integrated consumer campaign called "What the Flood!" and "Go-Bag Disaster Prep" in 2019. This award-winning consumer awareness program is focused on understanding, mitigating, and covering the risks associated with natural disasters to improve the availability and affordability of property insurance.

In 2021, the NAIC's CIPR conducted a survey to identify the steps consumers would be willing to take to reduce losses. Interestingly, more than two-thirds of consumers are aware of actions they can take to protect their property, but only half had made changes.

To encourage consumers to take steps to mitigate risks, the NAIC expanded its consumer campaigns to help people understand and reduce their risks and what they can do about them. The resources include comprehensive guides on selecting policies, interactive tools and social media campaigns, and a home inventory app with guidance for submitting claims.

The NAIC works with federal agencies like the Federal Emergency Management Agency (FEMA) and the Federal Alliance for Safe Homes (FLASH) to help generate awareness and create new material. FEMA and the NAIC worked together to generate consumer awareness around preparedness, including participation in two Twitter chats. The NAIC also contributed to the creation of FLASH's *Buyer's Guide to Resilient Homes*.



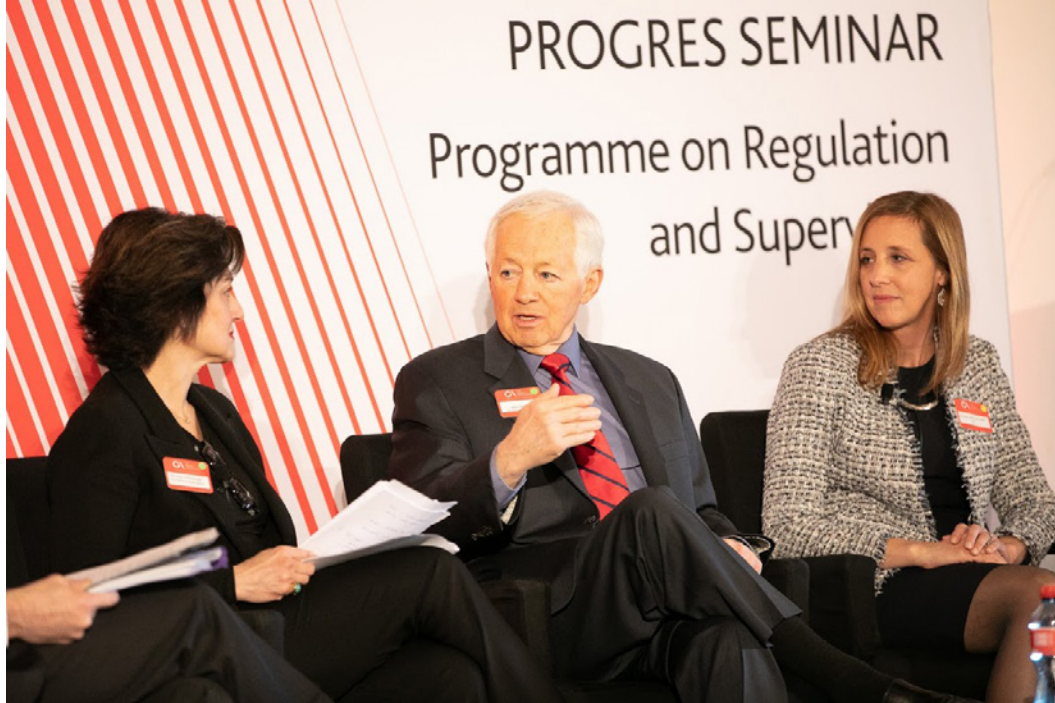
South Carolina Department of Insurance Director Raymond G. Farmer helps a homeowner make his home less vulnerable to storms.

Assisting consumers and protecting policyholders is a fundamental principle of insurance regulation. The NAIC supports state insurance departments across the country to help impacted communities both before and after disasters occur.

- An NAIC Disaster Assistance Program is available to states, providing support for data collection, consumer assistance call centers, and business continuity planning.
- The NAIC Complaints Database System (CDS) can be used by states to watch for trends in consumer complaints with companies.
- A Catastrophe Resource Center was created to provide state insurance regulators with resources for disaster preparation and response.
- Collectively, through the NAIC, state insurance regulators designed a Disaster Response Plan to share information and lessons learned regarding critical support services needed in the aftermath of severe weather events, including consumer assistance, call centers, and business continuity planning.

State insurance regulators continue to improve regulation in the best interest of insurance consumers and the public.





Washington Insurance Commissioner Mike Kreidler shares his thoughts on climate-related risks and mitigation.

Partnering Domestically and Internationally

NAIC members have been actively coordinating with state, federal, and international counterparts on climate-related risks. There's a long history of strong relationships between state and federal emergency managers and insurance regulators. The NAIC hosted regular workshops with FEMA in 2020 to collaborate on emergency management before disasters occur. The NAIC and FEMA also executed a Memorandum of Agreement (MOA) and formed an advisory group to assist state insurance regulators in collaborating with FEMA on an ongoing basis.

The NAIC has engaged with the U.S. Department of the Treasury (Treasury Department) through the Financial and Banking Information Infrastructure Committee (FBIIC). The FBIIC facilitates the sharing of information among federal and state financial regulators, particularly in response to incidents affecting the financial sector's infrastructure, including natural catastrophes.

President Joe Biden's Executive Order on climate risk directed the Financial Stability Oversight Council (FSOC) to examine and assess climate-related financial risk, and the NAIC and a designated state insurance commissioner have participated directly in those discussions.

Managing climate risk is a topic of many of the regulator-to-regulator bilateral dialogues facilitated by the NAIC for state insurance regulators. Internationally, the NAIC and its members actively participate in a variety of workstreams. This includes contributions to drafting climate-related supporting material and participating in strategic discussions. In 2020, the NAIC became a member of the Sustainable Insurance Forum (SIF).

Next Steps

When disaster strikes, long after the news coverage dies down and national attention turns elsewhere, state insurance regulators remain on the ground helping policyholders rebuild and local communities recover in the wake of climate-related loss. This is a personal issue for NAIC members because they are part of the communities where these events are taking place. It affects their friends and families.

Climate risks affect local communities but have global reach, so it will be crucial that state insurance regulators continue to keep pace with the challenges, leverage existing tools, and work together to address climate-related risks domestically and internationally.

The NAIC and state insurance regulators have a long history of working together to manage the economic consequences of climate-related events and a strong foundation of solvency and consumer protection tools that incorporate climate-related risk, which will continue long into the future.

Similarly, the NAIC is accustomed to providing expertise and other resources to state insurance regulators to support their effective regulation of the industry in a rapidly changing environment. As with any risk that affects the insurance industry, the NAIC is ready to assist state insurance regulators in developing the knowledge, expertise, tools, and resources needed to effectively regulate their markets. Using an inclusive and comprehensive approach will strengthen the insurance sector and help ensure that policyholders, especially the most vulnerable, are better protected from the devastating effects of climate-related risks.



State insurance regulators learn about the impact high winds can have on a structure.



Insurance commissioners visit IBHS to learn about mitigation techniques and FORTIFIED building materials.

What is the NAIC?

The National Association of Insurance Commissioners (NAIC) is part of the state-based system of insurance regulation in the U.S., and it provides expertise, data, and analysis for insurance commissioners to effectively regulate the industry and protect customers. Through the NAIC, state insurance regulators establish standards and best practices, conduct peer reviews and coordinate regulatory oversight. NAIC staff support these efforts and represent the collective views of state regulators domestically and internationally.



Shopping carts and building remains from the Camp Fire, which destroyed much of the town of Paradise, CA.

Dictionary

A list of key terms and organizations related to climate risk and resilience:

CATASTROPHE COMPUTER MODELING HANDBOOK

Adopted in 2010 to explore the use of catastrophe models in insurance to modernize the way state insurance regulators interact with and obtain information from catastrophe modelers. https://content.naic.org/sites/default/files/inline-files/prod_serv_special_ccm_op.pdf

FINANCIAL CONDITION EXAMINERS HANDBOOK

State insurance regulators examine insurers on a periodic basis to verify and validate their financial condition. The NAIC's *Financial Condition Examiners Handbook* is a guide to assist state insurance regulators in establishing and operating effective examinations, and it is continuously revised to reflect updated guidance in support of new regulations and emerging risks. https://content.naic.org/cmte_e_fehtg.htm

INSURER CLIMATE RISK DISCLOSURE SURVEY

An NAIC survey adopted in 2010 to identify trends, vulnerabilities, and best practices by collecting information about how companies assess and manage risk. <http://www.insurance.ca.gov/0250-insurers/0300-insurers/0100-applications/ClimateSurvey/>

OWN RISK AND SOLVENCY ASSESSMENT (ORSA)

Adopted as part of the NAIC's *Risk Management and Own Risk and Solvency Assessment Model Act (505)*, the ORSA is a tool to carry out risk-focused surveillance. It provides information about insurer risk exposure, including how they manage and control their risks and financial resources to cover

unexpected losses. The model requires insurers (above a specified premium threshold) to implement a risk management framework, prepare an ORSA, and file an annual report with their lead state supervisors. https://content.naic.org/cipr_topics/topic_own_risk_and_solvency_assessment_orsa.htm

RISK-BASED CAPITAL (RBC)

A fundamental tool for monitoring capital adequacy. The NAIC's RBC formula determines the minimum amount of capital an insurer should hold based on its risk profile. State insurance regulators continually update RBC charges to address the evolving risk landscape. https://content.naic.org/cipr_topics/topic_riskbased_capital.htm

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