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Written Testimony of

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Before the Connecticut General Assembly
Committee on Insurance and Real Estate

SB 1047, An Act Concerning Insurance and Climate Change

On behalf of Public Citizen, a national public interest advocacy group with more than 500,000 members and supporters, we welcome the opportunity to offer written testimony on SB 1047, an Act Concerning Insurance and Climate Change. Adopting this bill's disclosure and regulatory approach would establish Connecticut as a leader in managing the risks of climate change to the insurance market, an area where state insurance regulation has lagged global best practices. As the effects of climate change become worse every year, we strongly encourage the Committee on Insurance and Real Estate favorably report this bill and the Connecticut General Assembly to quickly pass it into law.

U.S. insurance companies are highly vulnerable to climate risk.

Climate change is already affecting the insurance industry adversely on both sides of insurers' balance sheets, and in turn it is harming policyholders. On the underwriting side, it is well-known that climate change is increasing the frequency and severity of catastrophic events such as wildfires and hurricanes. Less appreciated are harms that do not grab headlines but create losses, such as extreme heat, severe downpours and winds that strain infrastructure, and increased disease and violence, among others. Property and casualty (P/C) insurers typically state that they are not very vulnerable to these types of "physical" climate risks because they have short-term contracts, usually one year in duration, and can reprice them or discontinue coverage. Indeed, in response to unprecedented wildfires in the western United States over the past few years, P/C insurers have been exiting fire-prone regions. These plans to raise prices and exit markets may harm other financial institutions, policyholders, financial stability, and the broader economy.

Liability risk also could come into play. There are many attempts to hold fossil fuel companies accountable for climate change in court. Some may eventually gain traction, especially if norms continue to shift sharply toward climate solutions and against fossil fuels.

On the investment side, continued investment in fossil fuels exposes insurers to "transition" risks from falling asset prices and worthless stranded fossil fuel projects. A 2020 Moody's report found insurers' retreat from coal as "credit positive, as it protects them against potential climate change liability risk, and reduces the risk of their investment assets becoming 'stranded.'"[1] In other words, the market views coal exit policies as an important component of long-term insurer viability.

Insurers also increasingly face reputational risk from their fossil-fuel underwriting and investments as campaigners pressure them to abandon these activities. Globally, at least 23 insurers representing 12.9% of the primary and 48.3% of the reinsurance market have ended their cover for coal. Nine have exited tar sands. At least 65 insurers with combined investments worth $12 trillion have adopted divestment policies of some kind.[2]

[1] Moody's – Insurers' retreat from coal is positive, reducing stranded asset risk, limiting liability risk, Feb. 24, 2020.

[2] David Mason & Peter Bosshard, *Insuring Our Future, The 2020 Scorecard on Insurance, Fossil Fuels and Climate Change*, https://www.insureourfuture.us/s/2020-Insurance-Scorecard.pdf.

U.S. insurers lag their international counterparts in addressing climate risk. As of 2020, only one major American insurer was among the leaders on coal exit, while six major American insurers, including Connecticut-domiciled Travelers, brought up the rear.[3] Many major U.S. insurers continue to underwrite coal and oil and gas without any restrictions, and every major U.S. insurer supported lobby organizations that oppose climate actions.[4] This behavior exposes U.S. insurance companies to ever-increasing physical, transition, and reputational risks. Without regulatory intervention, it is unlikely that these insurance companies will reverse course and adopt prudent climate policies.

U.S. insurance regulators have not properly addressed the risk that climate change poses to insurance markets.

U.S. state insurance regulators are also well behind in adapting to climate risk. The Connecticut Insurance Department ("the Department") and five other states' insurance regulators administer the National Association of Insurance Commissioners (NAIC) Insurer Climate Risk Disclosure Survey to insurers licensed in those states. This survey was designed in 2009 and has not been updated since. Analysis by the American Academy of Actuaries shows that the current survey format yields only the bare minimum reply from the majority of insurers that are not participating in a voluntary disclosure standard. The NAIC is in the process of revising the survey, but the revisions will take time and are not guaranteed to yield disclosures in line with those proposed in this bill.

In the U.S., only New York State's Department of Financial Services has gone beyond disclosure and instructed that it "expects all New York insurers to start integrating the consideration of the financial risks from climate change into their governance frameworks, risk management processes, and business strategies."[5]

In contrast, the Bank of England's Prudential Regulation Authority included an "exploratory exercise" on climate in its 2019 stress tests for insurers, [6] and it planned to initiate climate stress tests in 2020 but postponed them until 2021 due to COVID-19.[7] The European Insurance and Occupational Pensions Authority requires insurers to provide detailed disclosures on environmental matters, including the proportion of their assets

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[3] 2020 Scorecard at 8.

[4] 2020 Scorecard at 9.

[5] New York Department of Financial Services, Insurance Circular Letter No. 15 (2020), Sept. 22, 2020, https://www.dfs.ny.gov/industry_guidance/circular_letters/cl2020_15.

[6] Bank of England, *Insurance Stress Test 2019*, Aug. 16, 2019, https://www.bankofengland.co.uk/prudential-regulation/letter/2019/insurance-stress-test-2019.

[7] *See* Alastair Marsh, *Bank of England Postpones Climate Stress Tests to Focus on Virus*, Bloomberg, May 7, 2020, https://www.bloomberg.com/news/articles/2020-05-07/bank-of-england-postpones-climate-stress-tests-to-focus-on-virus; *The Bank of England is Restarting the Climate Biennial Exploratory Scenario*, Nov. 13, 2020, https://www.bankofengland.co.uk/news/2020/november/the-boe-is-restarting-the-climate-biennial-exploratory-scenario.

invested in sustainable activities, as well as the proportion of their underwriting exposure associated with sustainable activities.[8]

With the threat of climate catastrophe continuing to increase, even as the transition to green energy accelerates, state insurance regulators must act now to assess the threats to the insurers they oversee and protect policyholders and insurance markets from climate risk. Disclosure is an important first step. To protect policyholders and markets, regulators need adequate information about insurers' exposure to climate risk, the governance and controls they have in place to manage those risks, and their contributions to GHG emissions, which will serve to exacerbate the risks that insurers face.

But disclosure will not be enough. To date, disclosure alone has not spurred sufficient action in jurisdictions where it is mandatory. Regulators must also use the tools at their disposal to directly oversee how insurers manage their own climate risk and contributions. Only this level of involvement can protect consumers and the insurance market from the cascading effects of climate harm.

The bill represents a major step forward in U.S. insurer reporting requirements.

A successful reporting regime needs to reveal the extent of an insurer's climate exposure and contribution, and how it is managing those risks. For the reporting to be useful and meaningful, it must provide standardized information that can be compared across insurers and must be publicly disclosed. Reporting requirements lacking these features will leave gaps in the ability of regulators and the public to assess an insurer's riskiness.

The reporting required by this bill addresses one of the major challenges for standardized disclosures: understanding the future impacts and risks of current activities.[9] Few metrics exist today, and those that do often lack a consistent methodology. Given these difficulties, some insurers may object that reporting on this information in a standardized way is not feasible or that publication could mislead the public about the scope of an insurer's climate exposure.

The bill strikes the right balance by requiring public disclosure of informative metrics that all insurers can measure today, while leaving room for the Department to update disclosure requirements as new metrics become available.

First, the bill requires disclosure of all investments by an insurer in fossil fuels, a good measure of future transition risk. These investments are at high risk of declining in value and ultimately becoming stranded assets as the world transitions to a low-carbon economy. Today, American insurers have $90 billion invested in coal.[10] As the transition accelerates, it will threaten solvency of insurers that are heavily invested in coal and other fossil fuel assets.

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[8] *The Future of Climate change Risk Regulation for Insurers in America?*, The National Law Review, Mar. 12, 2021, https://www.natlawreview.com/article/future-climate-change-risk-regulation-insurers-america.

[9] TCFD, Forward-Looking Financial Sector Metrics Consultation, Oct. 2020.

[10] Chris Seekings, *U.S. Insurers still have $90bn invested in coal*, The Actuary, Feb. 24 2021.

A thorough accounting of these exposures will provide transparency regarding which insurers are most at risk.

Second, the bill requires disclosure of gross premium underwriting for insureds involved in the fossil fuel industry and related industries. Fossil fuel companies' responsibility for greenhouse gas pollution is increasingly resulting in litigation seeking compensation for environmental harms and the effects of climate change from both governments and citizens. Given the increasingly precarious financial position of these companies, insurers may be left compensating the plaintiffs. The Department can use fossil fuel underwriting to monitor insurers for threats to their solvency from this potentially massive liability. This liability is compounded by the fact that the physical harms from climate change will also lead to an increase in claims by other clients, further pressuring insurer solvency and increasing insurance costs borne by consumers. In addition, the reputational risks from fossil fuel underwriting are growing, as some insurers have begun to note.

As climate science advances and the Department develops expertise from its initial rounds of climate risk supervision, new metrics can be added that more fully illuminate insurers' exposures to climate risks. Such metrics might include exposure to high emissions industries other than fossil fuels in both investment and underwriting, as well as more sophisticated modeling of physical risks to insurers' portfolios.

The bill also appropriately moves past disclosure to regulation of climate risk.

Once insurers begin adequately disclosing their climate risk exposures, the Department will need to supervise how they are managing and addressing those risks. This means integrating climate risk into the major tools used to supervise insurers today. These tools should include integrating climate risks into risk-based capital requirements, reviewing governance and internal controls to determine if they appropriately incorporate climate risk, and updating own risk and solvency assessment guidelines to take climate risk into account.

Equally important for protecting insurance markets will be aligning insurer activities with the goals expressed in the Paris Agreement to limit the increase in global average temperature to 1.5°C. Exceeding this target will result in more severe physical harms like extreme weather, increased flooding, and heat stress. The worse these effects, the greater the cost to insurers and policyholders. The Intergovernmental Panel on Climate Change has concluded that achieving this goal will require net zero global emissions by 2050, with reductions of at least forty-five percent by 2030.[11] Insurers that provide fossil fuel cover above what would align with Paris targets contribute to the future risks the insurance market and policy holders will face.

By requiring the commissioner to submit an annual report on efforts in these areas, this bill clarifies the Department's mandate to address climate risk and emissions contribution as part of its regulation and supervision of insurers. The General Assembly should use the

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[11] Intergovernmental Panel on Climate Change, Special Report: Global Warming of 1.5°C, https://www.ipcc.ch/sr15/.

annual report process as an opportunity to track the Department's progress and update both the disclosure and supervision requirements based on the progress of Connecticut-licensed insurers.

Conclusion

Adopting this bill will put Connecticut on the forefront of climate risk regulation of insurers and give it an opportunity to serve as a role model for other U.S. states and the world. The requirements will also give a competitive boost to Connecticut-licensed insurers, in line with a recent Societe General report's finding that an insurer's position on coal underwriting and investments affects its valuation by -3% to +9%.[12] Delay on vigorous climate risk legislation will harm not only the planet, but the future prospects of the Connecticut insurance industry. We encourage the committee to favorably report this bill and the General Assembly to adopt it as quickly as possible.

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[12] Tim Quinson, *As Insurers Exit Coal Underwriting, They May Find It's Good for Stock Valuations*, Insurance Journal, Feb. 2, 2021, https://www.insurancejournal.com/news/international/2021/02/02/599641.htm.