U.S. Chamber of Commerce

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International Association of Insurance Supervisors
c/o Bank for International Settlements
CH-4002 Basel
Switzerland

To Whom It May Concern:

The U.S. Chamber of Commerce ("the Chamber") is pleased to respond to the International Association of Insurance Supervisors' ("IAIS") public consultation on climate risk supervisory guidance ("the consultation"). While the Chamber agrees that climate change is a source of risk that insurers should account for, we question the implication that climate change is currently a financial stability risk to the insurance sector.

The Chamber has long supported practical, flexible, predictable, and durable market-based solutions to address climate risk. Our members are driving private sector innovation across industry sectors that will be central to solving climate change.

To ensure optimal policy outcomes, the best science and observations available, identification of material risk, and a rigorous assessment of available alternatives through cost-benefit tradeoffs should be the drivers of climate-related financial services policy. Billions of dollars in private sector research and development have led to the creation and implementation of innovations that help manage climate risk, accelerate emissions reductions, and help communities and companies adapt and build resilience; the insurance industry has been at the leading edge in addressing the impacts of climate change for years. Insurers have undertaken voluntary actions to address climate-related financial risk, including changes in underwriting, promoting resilience and predisaster mitigation for at-risk assets, and changes in long-term investment strategy to prepare ahead of the next crises.[1] The Chamber is committed to addressing these challenges with market-centered solutions and welcomes the opportunity to engage in constructive collaboration towards these ends.

The consultation rightly notes that "the insurance industry plays a critical role in the management of climate-related risks in its capacity as an assessor, manager

[1] U.S. Chamber of Commerce comments to the Federal Insurance Office (November 15, 2021) Found at: http://www.centerforcapitalmarkets.com/wp-content/uploads/2021/11/U.S-Chamber-of-CommerceComments_InsuranceSectorClimateFinancialRisks_Treasury-PDF.pdf?#

and carrier of risk, and as an investor and steward of financial resources, while being uniquely qualified to understand the pricing of insurance risks." Climate risk is among a host of risks that insurers account for in their strategic planning, and insurers employ different strategies to prepare for each type of risk. For decades, insurers have been at the leading edge of demonstrating significant understanding of climate risks and have been integrating strategies to address climate-related risk throughout their organizations over various time horizons. Insurers are also reducing risks over the life cycle of their assets by making investments in more smart, modern, resilient infrastructure. Upcoming consultations by IAIS should focus on how supervisors and insurers are considering climate risk in their planning and risk management processes. Any future material developed by the IAIS should not create an expectation of "one-size-fits-all" mandates but should highlight how climate-related risk is being contemplated over different time horizons.

The consultation states that climate change and climate-related risks are material for the insurance sector, and the Executive Summary asserts a linkage between climate risk and financial stability. Climate change is certainly a risk that insurers should identify and manage, and they have the tools to do so. In fact, the insurance industry has been including climate risk in long-term planning for years. Moreover, the consultation appears to conflate insurer financial stability concerns with protection gaps. The tools a supervisor would use to mitigate financial stability risks generally involve actions that reduce exposure to such risks. However, the IAIS's concerns with increasing protection gaps as climate reduces insurability is generally solved by solutions to increase exposure to fill such perceived gaps, thereby potentially exacerbating risks to an insurer's financial condition.

In addition, we are concerned that an undue focus on climate risk could lead both insurers and regulatory authorities to place less emphasis on more immediate and material risks. Since climate risk is a long-term risk and it is unclear how and to what degree such risks will come to fruition, an inordinate emphasis on these risks and using resources toward that end could lead insurers to neglect more serious near-term risk. We ask the IAIS to strike the right balance in its focus on climate risk.

The plausibility and certainty of a risk are key considerations for insurers in determining whether a risk is material. Insurers' boards and management will place greater attention on risks that meet these criteria. If a company determines that risks are speculative and distant, they generally will not consider them material or give them heightened scrutiny, and companies should be given the flexibility to determine whether risks are material. In any future recommendations, we urge the IAIS not to place any undue emphasis on climate-related risks over others in a financial institution's overall risk strategy, which could lead the institutions to spend disproportionate time and resources on climate risks when others may be more material.

The consultation also asks about transition plans and whether the IAIS should explore those in a future consultation. We do not believe that transition planning merits further IAIS work at this time given the IAIS' role as a prudential regulatory standard-setter rather than a climate regulator. To the extent climate risk can be a driver for financial risks on a firm's balance sheet, the evaluation of an insurer's management of climate transition and adaptation risks should be addressed as part of existing filings with supervisors like Own Risk and Solvency Assessment (ORSA).

We also caution the IAIS against any recommendations to supervisors on "greening the financial system." The Chamber agrees that climate risk is serious and that financial institutions need to account for and incorporate it into their risk management systems. However, we are concerned with the use of any tools at the disposal of regulatory bodies to "green the financial system," as this may distract insurers and regulators from safety and soundness considerations and their ability to meet the obligations of policy holders. Regulators' role is to understand and help financial institutions mitigate risk, which might manifest due to climate change.

We would also oppose any recommendations to supervisors on climate-related financial risk that are intended to shift capital away from industries or sectors that may have, or are perceived to have, more environmental risk. Markets, not political decisions, should determine underwriting, and such decisions should be risk-based. Any recommendations on shifting capital away from certain industries would be beyond the IAIS' role as a prudential regulatory standard-setter. We encourage the IAIS to limit its focus to supporting financial institutions in their assessment of climate risks only for micro or macroprudential purposes and not to recommend standards that would determine capital allocation.

The Chamber also supports a clear differentiation between climate scenario analysis exercises and traditional regulatory stress testing exercises[2], which typically

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[2] Bank Policy Institute (BPI), Challenges in Stress Testing and Climate Change (October 2020), https://bpi.com/challenges-in-stress-testing-and-climate-change/: "Stress testing for climate change is starkly different from existing macro stress testing and given data and methodology challenges likely to be less reliable. First, the lack of historical data creates important challenges in modeling the interactions between climate, the macroeconomy, and the financial sector, which are necessary requirements in designing plausible and coherent scenarios. Second, climate stress testing attempts to measure outcomes over a much longer time horizon—30 to 50 years rather than nine quarters for macroeconomic stress testing. Third, models that generally relate credit losses to climate risk scenarios require large amounts of information about future counterparty behavior over a long time horizon. Fourth, climate stress tests generally assume that banks take no actions to hedge or reduce exposures to climate risks over that horizon. While macroeconomic stress testing has a similar assumption

assess the potential impacts of transitory shocks to near-term economic and financial conditions. We oppose climate scenario testing for the purposes of imposing new prudential requirements and believe a more qualitative horizon scanning approach, particularly for longer time horizons is a more appropriate tool to help understand potential risks to a financial institution's balance sheet and inform its overall risk management strategy.

Finally, a major consideration for U.S. insurers is America's well-functioning system in which states (not the federal government) are the primary regulators of the insurance industry. For years, the insurance industry has been at the forefront in addressing climate change impacts. Insurers have voluntarily made changes in underwriting, promoted resilience and predisaster mitigation for at-risk assets insured by commercial P&C, and changed long-term investment strategies. Regulatory bodies, including the U.S. Federal Reserve Board have taken notice of these efforts and have recognized the health of the insurance industry in the face of climate-related risks.[3] The IAIS should build upon the work of the U.S. insurance industry and its state-based regulators in any forthcoming recommendations.

<u>Conclusion</u>

As the IAIS continues to assess climate risk in the insurance industry, it must recognize the remarkable progress the industry has made through market-based approaches and practices and increased communication between companies and their customers. Any climate risk proposals should allow insurers flexibility and should consider their particular business, operations, and financial performance.

We thank you for the opportunity to offer these comments and look forward to working constructively with you on these issues going forward.

Sincerely,

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regarding hedging, and therefore may produce some error over a nine-quarter horizon, this assumption, however, becomes deeply counterfactual over a period of decades."

[3] Board of Governors of the Federal Reserve System Financial Stability Report (November 2021) at 41. Found at: The Fed - Financial Stability Report – November 2021 (federalreserve.gov): "P&C insurers are one type of financial institution whose leverage may be affected by climate change. Leverage at P&C insurers remained at historically low levels in the first half of 2021. The low leverage allowed P&C insurers to cover claims from recent severe weather events without solvency issues."

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