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COMMENTS
OF
AMERICAN PROPERTY CASUALTY INSURANCE ASSOCIATION
ON
FSB SUPERVISORY AND REGULATORY APPROACHES TO CLIMATE-RELATED RISKS

The American Property Casualty Insurance Association (APCIA) represents nearly 1200 (re)insurers that operate in the U.S. and around the globe. Our membership is characterized by diverse business models and companies of all sizes that provide critically important insurance coverage and loss prevention services that provide significant benefit to policyholders and the public.

Need for Globally Consistent Standards

On behalf of our international members, APCIA supports the movement toward globally consistent climate risk supervision to reduce or eliminate supervisory or regulatory mandates that are repetitive or worse, are in conflict. A global risk demands a globally coordinated response, not more fragmentation. The supervisory standards should, however, be flexible enough in implementation so as to take into account differences in business models and liability regimes.

We note that in the U.S., a group of 15 states under the auspices of the NAIC have recently approved changes to the annual climate risk disclosure survey in line with the Task Force on Climate-related Financial Disclosures (TCFD) and that work should be referenced in the FSB document. The changes affect nearly 80% of the U.S. insurance market and were adopted after significant consultation with all stakeholders.

Response to Question 3: Definition of Climate-Related Risks

APCIA agrees the report appropriately identifies the elements of a common high-level definition of climate-related risks. However, this definition is overinclusive because it conflates weather and climate-related risks.

APCIA members collect meteorological data regarding weather-related events and analyze long-term trends based on that data in combination with socio-economic developments and loss to identify indications of changing risk (increasing losses) from weather-related events. Research methods enable scientists to state whether, in a specific region, extreme events (such as rain above a certain amount or temperatures above a certain threshold) have become more or less likely, compared with a world without climate change. At the same time, attributing an event or a portion of an event directly to climate change is not possible, given the varying factors and underlying assumptions.

Because the proposed rules conflate weather and climate-related events, the resulting disclosures likely would overstate the effects of climate change. The final definition of climate-related risks should acknowledge that companies are not able to determine the extent to which weather events or natural conditions simply represent weather or are exacerbated by climate change.

Responses to Questions 1-4: Data Collection

We support the efforts by policymakers and standard-setters to develop a well-harmonized and evidence-based approach to assessing potential climate risk across the insurance sector and financial services more broadly. However, we caution against initiating overly granular data gathering exercises on an accelerated basis, particularly if targeting information that does not align with existing management and financial reporting systems. Beyond the operational burden of premature data calls – which could distract from other, higher-priority industry initiatives to assess and address climate risk – it will also become increasingly difficult for regulators to discern "signal" from "noise" if inundated with still-nascent forms of climate data. We therefore encourage the jurisdictional regulators – perhaps with the assistance of global regulatory standard setting bodies such as the FSB or IAIS – to coordinate as much as possible on the design and execution of surveys, information requests and stock-takes and more distinctly determine the rationale of potential data and metrics for assessing climate risk, by linking each desired data item with a description or explanation of how that particular information supports or promotes their monitoring objectives.

A. We note that the paper references supervisors' use of surveys, information requests and stock-takes in order to gain a better appreciation and understanding of financial institutions climate-related risk exposures. Our experience was that we ended up receiving numerous and highly duplicative surveys.

B. Table 1 (in connection to recommendation 1) is instructive insofar as it highlights the breadth and scope of information that has been collected by various jurisdictional regulators. This underscores the point above around the need supervisors to set clear and transparent objectives with regards to their information requests and to coordinate amongst themselves to the fullest extent possible.

Responses to Questions 1-4: Data Reliability

We want to caution against the view (Section 2.2 in particular) that strong(er) governance, processes and controls at the financial institution-level will alone solve for the reliability of climate-related data for internal and external reporting purposes. The FSB report seeks to gather climate-related information that is simultaneously granular, reliable, and comparable – and to do so in an accelerated manner. However, particularly given the evolving state of climate-related data analysis and disclosure, there could be inherent tensions between these objectives. For example, highly granular data (for example, on a local geographical basis) might not be sufficiently reliable as it is heavily dependent upon data provided by non-financial corporates who are our insureds and investees. Similarly, such granular data may not be readily comparable across a broad range of insurance and financial services companies.

A. There are multiple climate risk-related data points (e.g., Scope 3 emission) where there is general acknowledgment that a significant error band exists at least over the near-term and for which only "limited assurance" can be obtained from, for example, external auditors.

Responses to Questions 5-7: Systemic Risk

Insurance regulators should assess the potential impact of climate risk on financial stability by applying the IAIS holistic framework, which delineates a coherent process and mechanism for identifying vulnerabilities, corresponding transmission mechanisms, and mitigating factors. Climate risk is certainly meaningful and relevant to insurers' investment and liability management. That said, we believe that the design of prudential tools for addressing potential systemic vulnerabilities related to climate risk would benefit from a more structured assessment, including a stronger definition of how asset "fire sales" or exposure-related shocks could result from climate risks. While we recognize that certain aspects of the evolution of climate risk involve horizon scanning – and are therefore challenging to define with precision at this stage – we would note that part of the FSB's assertion of climate-related systemic risks are largely anecdotal in nature.

Responses to Questions 5-7: Scenario Analysis and Static vs. Dynamic Balance Sheets

On climate scenario analysis exercises, we strongly support efforts to help coordinate these exercises either on a cross-jurisdictional basis or perhaps centrally coordinated via global regulatory standard setting bodies.

A. We caution supervisors about drawing firm conclusions from the exercises particularly over the longer time horizons and by extension using results to guide supervisory actions

B. Significant commitments in terms of resources

    I. Use of static balance sheet scenarios ought to be limited, targeting a narrow set of objectives. We agree with the point (under section 4.2.2) that over shorter-term time horizons there is some usefulness in running static balance sheet exercises. We further believe that depending upon objective(s), there may also be certain instances where a static balance sheet makes sense when running longer-term scenarios such as where the intent is to isolate for certain climate inputs that are of particular interest. It is also helpful in the context of aggregating results across many participants.

    II. Notwithstanding point B above, Assets on insurers' balance sheets roll-over frequently thus use of a static balance sheet approach, particularly over the longer-term time horizons, introduces significant limitations in terms the conclusions that can be drawn from the exercise

Response to Question 9: Need to Recognize Critical Elements of Sound Supervision and Regulation

The elements we discuss below have been incorporated in the recent U.S. state action mentioned above and could serve as an example. Many of the elements are also reflected in the OECD's "Policy Framework for Effective and Efficient Financial Regulation". We therefore request that these elements be included in the final version of the document.

APCIA's core environmental principles call for supervisory and regulatory standards that recognize legitimate needs of firms for confidentiality, especially for forward looking information. APCIA would appreciate more discussion about the importance of confidentiality and the protection of intellectual property.

It is critically important to recognize proportionality in standard setting and implementation. Supervision and regulation should be flexible enough to take into account the nature, scale and complexity of the diverse businesses being supervised. For example, the time horizon for underwriting and investing in much of the property and casualty insurance sector is comparatively short-term and therefore insurers have the ability to quickly adjust pricing, accordingly, given changing climate conditions. Furthermore, insurers can adjust balance sheets (Asset Liability Matching) to address evolving climate risks, subject to supervisory and regulatory capital and liquidity constraints.

Materiality is another critically important aspect to be taken into consideration. Basing supervision on what is truly material to a firm will help assure that the desired objectives are achieved, and that the compliance exercise and the results thereof will also be beneficial to the firm.

Supervisory standards and requirements should be flexible enough to recognize differences in litigation and liability regimes. The same disclosure that in one jurisdiction has only up-side consequences could carry significant downside consequences in other jurisdictions including misinterpretation of disclosures that could result in unjustified reputational damage.

Supervisory standards and requirements should be based on a cost/benefit analysis. It should be well established for any mandates that the benefits to the firm and society at large far exceed the cost of compliance. Further, such analyses also help identify any unintended negative consequences, such as a reduction in innovation and/or competition that ultimately does not benefit supervisors and consumers. Policymakers and supervisors should recognize that the transition to net-zero is an evolution and cannot be achieved immediately and also requires a public-private partnership in addressing financial risks from climate change.

Conclusion

We respectfully request consideration and inclusion in the document of the elements we have outlined above so as to provide supervisory guidance that will achieve the best outcomes for supervisors, firms, and the public. We would be pleased to provide any additional information.

Respectfully submitted,

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