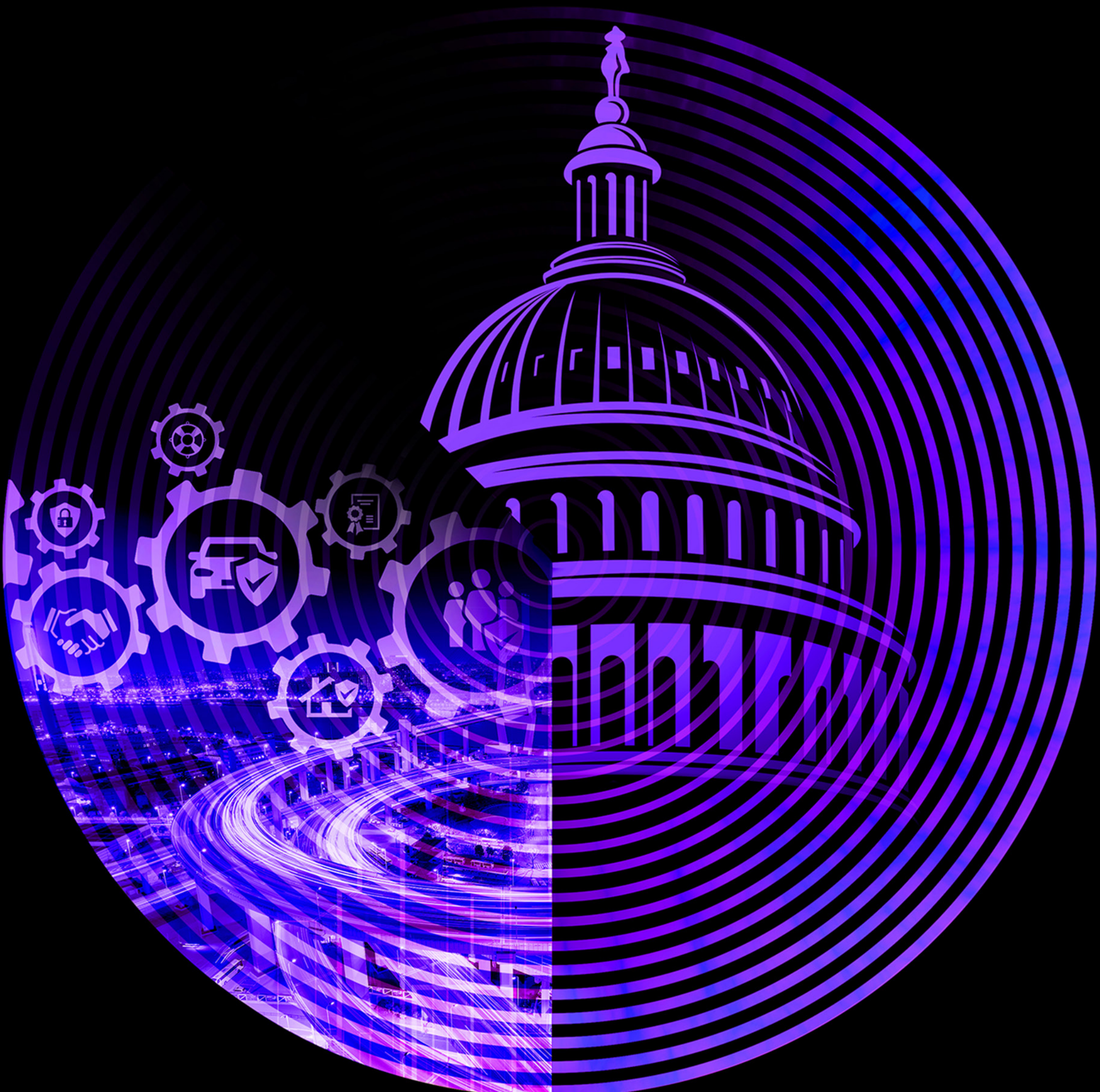
Deloitte.



NAIC's flagship international event brings focus on coverage gaps amid a swift-moving but still-stable sector

Center *for*
Regulatory Strategy
US

Contents

Introduction

The National Association of Insurance Commissioners (NAIC) International Insurance Forum held May 18–19 in Washington, DC, was the premier spot to both be and be seen in the US insurance regulatory realm this spring for those with a bent toward global supervisory topics of the day.[1]

The forum, now in its 16th year, was the hottest ticket in town. It was not only sold out but boasted a waiting list of many people hoping to get a seat at one of the roundtables in the deep basement of a popular Capitol Hill hotel.[2] Most were able to be accommodated, and attendance reached almost 300 attendees, the NAIC informed.

With the late spring International Association of Insurance Supervisors (IAIS) Global Seminar going virtual, this spring event in DC will become the signature international insurance supervisory meeting.

NAIC President and Commissioner of the Missouri Department of Commerce and Insurance Chlora Lindley-Myers even joked that the conference was "almost as hot a ticket as a Taylor Swift concert."

The forum highlighted strengths of the insurance industry and its position globally—but also drew attention to various gaps that it might need to fill.

The two-day conference, emceed by Massachusetts Insurance Commissioner and NAIC International Insurance Relations Committee Chair Gary Anderson, kicked off with Federal Reserve Governor Philip Jefferson remarking on how the insurance industry has performed well through recent stress.

Volatility abounds, but insurance capital guardrails keep sector stable

Jefferson pointed out that although profitability in the Property & Casualty (P&C) industry was reduced in 2022 by natural catastrophes and inflation, the sector's capital appears strong when considering a range of plausible stress events. On the life insurance side, Jefferson called the recent increase in interest rates a most welcome development in that it has allowed for higher investment returns, but he cautioned that the situation also poses risks for early withdrawals by some policyholders.

Jefferson also took slight aim at the use of reinsurance vehicles for life insurance capital, saying its use "merits continued monitoring." [3]

Economic volatility continued as a macro theme, with Jefferson acknowledging that progress on inflation remains a challenge.

Later, IAIS Secretary General Jonathan Dixon appeared to affirm Governor Jefferson's conclusions by noting that the insurance sector had remained stable through the recent volatility in the banking sector, but the IAIS is studying the lessons learned. He noted that direct exposures to banks vary across jurisdictions across the world and stressed the important of good asset-liability matching. Of course, the IAIS will be interested in analysis on any margin calls and the downside of rising interest rates. He also recognized that private equity's pursuit of excess yield from potentially volatile products could be a concern.

Identifying and remedying coverage gaps

Insurance regulators and industry leaders turned inward throughout the forum to discuss insurance coverage gaps from training and education gaps, to communication gaps, to protection gaps across all lines of insurance, including everything from cyber coverage to essential insurance products at the community and individual level. There was even discussion of hidden gaps, ones that might not be readily identified.

During a panel entitled "Views from the C-suite—Opportunities and Challenges for the Road Ahead," moderated by Lindley-Myers, one insurance company executive said that although she did not see gaps on the regulatory side, she believes there is a gap that exists on the part of small business owners in their perspective on cyber insurance coverage.

In a panel moderated by Andrew Mais, NAIC president-elect and commissioner of the Connecticut Insurance Department, consumer advocates, P&C industry risk executives, and regulators discussed protection gaps for hazards such as wind risk and flood insurance. One industry panelist noted that it is a necessary first step for an agent to explain peril risk to homeowners and inform them about flood insurance grant programs to help cover the gap.

One insurance brokerage executive recommended the use of parametric insurance for flood events to help fill the gap, allowing for an immediate payout before the Federal Emergency Management Agency (FEMA) steps in. Parametric insurance, which pays out a certain amount that may not cover actual losses if a trigger event occurs and surpasses a certain damage amount, has a place among coverage options, he said.

A life insurance CEO noted that climate change acceleration, with its flooding effects in some areas, is close to the company's heart as he recalled when 2012's Superstorm Sandy displaced his colleagues for nine months after striking New York City and flooding the basement of the company's building.

At the same time, executives noted that on a global level, having flood insurance be optional for properties is unique.

Mais remarked that risks continue to grow around the world, with cyber, climate, and longer life spans, and addressed the "significant" need for both consumer education and risk mitigation to reduce overall cost.

Another insurance executive for a national auto insurance called out the need for talent in the industry, another gap that the industry is trying to address in recruitment efforts, even as companies explore and utilize artificial intelligence (AI) to a greater degree. Others joined in, discussing a dedication to develop talent while technology develops.

For instance, blind spots in cybersecurity keep one life insurance executive up at night, as he has told his board. "You inherently can't see blind spots," he said. He pointed out that there are 750,000 cyber jobs open in the United States, and hackers in one country that's been deemed a threat have a 50-to-1 ratio to Federal Bureau of Investigation personnel. "It's a threat to the entire economy. We have to address the skill gap" and be "training up more people on cyber," he said.

Innovation is also helping consumers and filling gaps in diverse ways, according to panelists at the forum.

AI is helping the insurer respond more quickly in the claims process by assessing the condition of a property, say, after a wildfire, a P&C insurance executive said. The executive acknowledged that some consumers would want to reach out to member services without going more digital, so the company will maintain that channel. "We are using [AI] as complementary … and still relying on a personal touch," she noted.

Meanwhile, the life insurance executive said products might reach more people by anticipating their needs and getting underwriting information from them through technology, without the usual "bloods and fluids" traditionally used as part of the life insurance underwriting process. Technology, he said, "will help us access communities that aren't being accessed today."

Insurance supervisors and industry executives also delved into gaps and how they were being addressed on the diversity, equity, and inclusion (DEI) front.

IAIS Secretary General Dixon said that financial inclusion has been a topic for the organization for more than a decade and has manifested most recently in its DEI imperatives.

Insurance sector continues to wrestle with technology implications

Insurance panelists also grappled with AI and the question of unfair discriminatory outcomes in models, as well as how regulators can decide what unfair bias is and is not, especially with technology moving swiftly among many (still) unanswered questions.

"I don't know what the answer is going to be," acknowledged one executive.

A tech industry representative, Dennis Noordhoek, director of public policy and regulation for The Geneva Association said his group, an international association of insurance companies, is currently working on a paper to "take the hype out of AI."

Panelists, including panel moderator Dean Cameron, NAIC's previous president and Idaho's insurance director, wondered about the role of consumers using data to reduce their risks, if they know what the data or algorithms reveal, and whether individual pricing isn't a bad thing after all, in the end. Insurers championed information and data to reduce risk, and many agreed that increased granularity doesn't mean there isn't risk pooling. In fact, one insurer argued, greater risk classification should make risks more insurable rather than less.

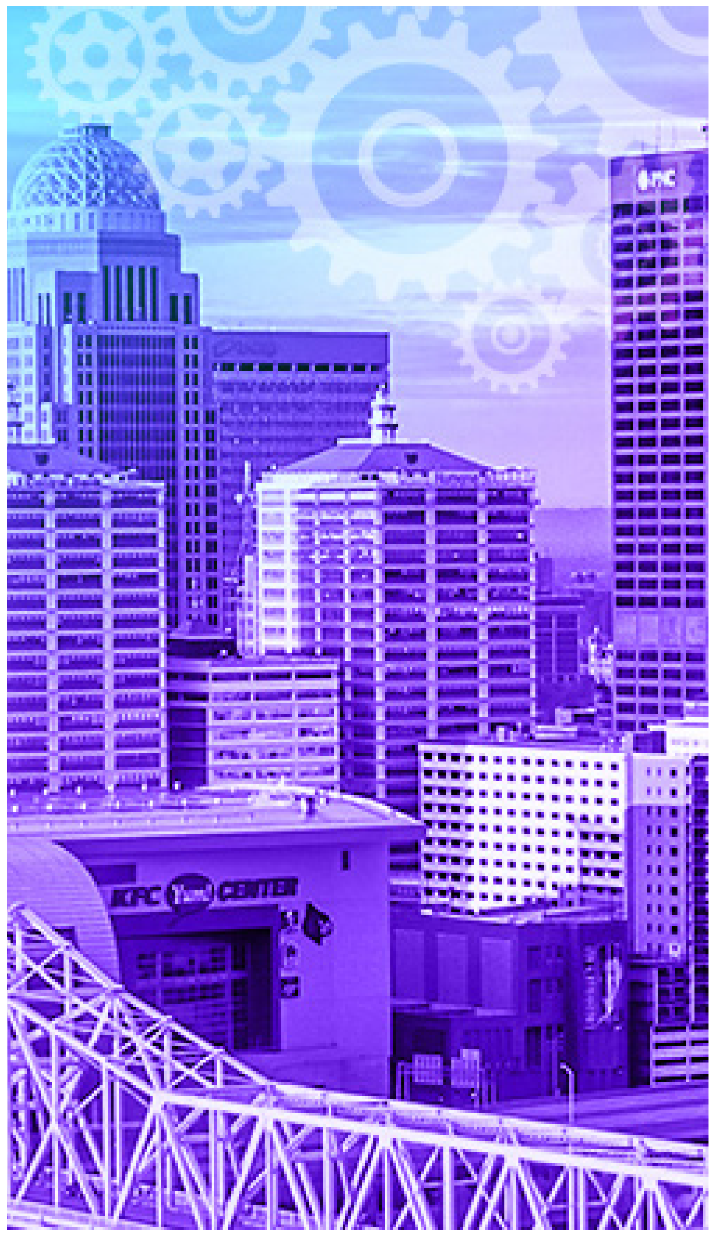
Cameron expressed concern about the creation of additional bias if consumers can't get products they need and the fact that they might not know about how they can reduce risk. "We visited with the consumer—their credit had not changed, but they were getting a significant rate increase," he lamented. Cameron weighed a query on whether data granularity wasn't instead undermining the pooled nature of insurance.

On a separate panel, when asked if AI could help with infrastructure investment by insurers with a multitrillion-dollar infrastructure gap in the United States alone, an industry investment expert retorted, "When it learns how to dig trenches and lay bricks."

Meanwhile, a panel devoted to cyber resilience and the fast-growing cyber insurance market underscored the trend toward a risk-based approach, where boards are starting to notice that cybersecurity is something they should actively oversee, as one tech executive pointed out.

Another trend at insurance firms is the growing relationship between the chief information officer role and the risk manager role. They are not converging so much as developing a stronger partnership than in the past, noted a tech company executive who works on business risk and insurance issues. She spoke of using generative AI and intel fed into a model to detect new threats.

Domhnall Cullinan, director of insurance supervision at the Central Bank of Ireland discussed the moral hazard involved in deciding whether to pay ransom in cyberattacks to nation-state malicious actors. This also enveloped the question of coverage from cyberattacks deemed actors of war, with participants discussing the uncertainty on cyber coverage globally, even as threats (and the coverage market for them) continues to grow.



Climate risk remains top of mind for supervisors and industry

Among the other topics of the day, climate risk remained a constant, sobering refrain.

Dixon and others returned to the subject as it unites all participants across sectors and disciplines. "Climate is the top priority for us at the moment," he told participants.[4] The IAIS had just closed an open stakeholder feedback period May 16 on its first such document "Public consultation on climate risk supervisory guidance," published in March 2023. The document proposes "a globally consistent supervisory response to climate change within the insurance sector," including potential changes to supporting supervisory material governance, risk management, and internal controls.[5]

One reinsurance company executive said she expects many changes on the climate front over the next few years, based on the data that comes in with scoring of the underlying carbon footprint of the company's portfolios, with better pricing for those who have a better carbon footprint score. The Bermuda-based P&C reinsurer was founded after Hurricane Andrew to take on insured losses.

Climate-related challenges and progress even beyond the discussion of coverage gaps also took center stage at the forum.

As insurers push forward to reduce their footprints or make sure all their buildings are LEED-certified, one investment strategy executive for a large global insurer cautioned that having a portfolio of all green holdings or all fossil fuels would be risky and counseled that insurers stay focused on diversifying portfolios.

Other panelists included global climate officers, CEOs, and general counsels, all poised to react to changing climate risk and data.

One auto insurance company executive noted that the company feels responsible in forging a financial relationship with its policyholders on catastrophic losses to reduce the risk of loss to them.

However, one investment professional said that its focus was on credit, paying back debt, and how the industry can handle it. "We don't care how many dolphins are saved," this person remarked, returning focus to the bottom line.

One auto insurance company executive noted that the company feels responsible in forging a financial relationship with its policyholders on catastrophic losses to reduce the risk of loss to them.

However, one investment professional said that its focus was on credit, paying back debt, and how the industry can handle it. "We don't care how many dolphins are saved," this person remarked, returning focus to the bottom line.

Looking ahead

Many US stakeholders are keeping their eyes on the prize—that is, the IAIS annual meeting in Tokyo in November, where discussions around the Insurance Capital Standard (ICS) will hold sway.[6] The ICS, a consolidated groupwide capital standard for international insurers, is undergoing a monitoring period which began in 2020.[7] At the May NAIC forum, the ICS was only lightly touched upon by Dixon, but he certainly identified it as a priority—it has been a decade in the making, after all. It was back in October 2013 when the IAIS first announced it would develop the ICS to judge capital adequacy in insurers operating globally.[8]

For US insurers, the homegrown methodology known as the aggregation method (AM) must pass muster based on criteria that assess whether it has comparable outcomes to the global ICS, a discussion which should provide for a lively annual meeting.

The Basel-based organization of insurance supervisors agreed on the criteria it will use to assess the AM methodology back in March. It said it would begin the comparability assessment in the third quarter of 2023, which means there should be much feedback by the fourth quarter, when the annual meeting in Tokyo is underway.[9]

By that time, the US hurricane season will have been underway with concomitant flooding and wind damage reports, deepening the discussion—and perhaps the urgency—on addressing climate change risk and affordability and availability from the US perspective.

The annual IAIS meeting will be bookended by two NAIC national meetings—one held August 12–16 in Seattle and the other November 30 to December 4 in Orlando.

Similar to last year, expect a consolidated report on IAIS international conference events.[10]

Endnotes

1 National Association of Insurance Commissioners (NAIC), "2023 International Insurance Forum," May 18–19, 2023

2 NAIC, "NAIC's 2021 International Insurance Forum starts today ... more than 500 scheduled to attend," press release, May 25, 2021.

3 Board of Governors of the Federal Reserve System (FRB), "The U.S. economic outlook and considerations for monetary policy," remarks by Philip N. Jefferson at the 2023 International Insurance Forum (Washington, DC, May 18, 2023).

4 International Association of Insurance Supervisors (IAIS), "Public consultation on climate risk supervisory guidance – part one," March 2023.

5 Ibid.

6 IAIS, "IAIS announces location for 2023 Annual Conference," April 7, 2022.

7 IAIS, "Insurance Capital Standard," June 30, 2022.

8 Ibid.

9 IAIS, "IAIS finalises criteria that will be used to assess whether the Aggregation Method provides comparable outcomes to the Insurance Capital Standard," press release, March 9, 2023.

10 Deloitte, "IAIS 2022 annual conference update," 2023.

Contacts

Karl Hersch
US Insurance Leader
Principal | Deloitte & Touche LLP
khersch@deloitte.com

Rich Godfrey
Principal | Deloitte & Touche LLP
rgodfrey@deloitte.com

David Sherwood
Managing Director | Deloitte & Touche LLP
dsherwood@deloitte.com

Josh Martin
Managing Director | Deloitte & Touche LLP
joshmartin@deloitte.com

Center for Regulatory Strategy Americas

Irena Gecas-McCarthy
FSI Director, Deloitte Center for Regulatory Strategy, US
Principal | Deloitte & Touche LLP
igecasmccarthy@deloitte.com

Jim Eckenrode
Managing Director | Deloitte Services LP
jeckenrode@deloitte.com

Liz Festa
Senior Research Analyst | Deloitte Services LP
lfesta@deloitte.com

Center *for*
Regulatory Strategy
US

About the Center
The Deloitte Center for Regulatory Strategy provides valuable insight to help organizations in the financial services industry keep abreast of emerging regulatory and compliance requirements, regulatory implementation leading practices, and other regulatory trends. Home to a team of experienced executives, former regulators, and Deloitte professionals with extensive experience solving complex regulatory issues, the Center exists to bring relevant information and specialized perspectives to our clients through a range of media, including thought leadership, research, forums, webcasts, and events.

This publication is a summary of the common themes expressed by the participants at the NAIC Spring National Meeting that took place March 21–25, 2023. The notes were taken informally and were based on discussions heard and were not validated or confirmed by Deloitte. Deloitte is not, by means of this publication, rendering accounting, business, financial, investment, legal, tax, or other professional advice or services. This publication is not a substitute for such professional advice or services, nor should it be used as a basis for any decision or action that may affect your business. Before making any decision or taking any action that may affect your business, you should consult a qualified professional adviser. Deloitte shall not be responsible for any loss sustained by any person who relies on this publication.

Deloitte.