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GOVERNMENT RELATIONS

Hearing Summary

June 5, 2024

SENATE BUDGET COMMITTEE HEARING ON THE IMPACTS OF CLIMATE CHANGE ON INSURANCE MARKETS

EXECUTIVE SUMMARY

On June 5, the Senate Budget Committee convened a hearing to discuss the impacts of climate change on insurance markets. Discussion among the senators present was generally divided along partisan lines, with Republicans rejecting the premise that climate change has had any significant impact on insurance rates or availability. For their part, Democrats were specifically focused on climate change in relation to homeowners' insurance and generally avoided discussion of broader issues related to climate change.

Notably, **Sen. Mitt Romney (R-UT)** agreed with Democrats in recognizing the importance of countering climate change and reiterated his calls for a global carbon tax, along with more targeted mitigation efforts. Democrats and Republicans were united in recognizing the potential risks posed to the wider financial system by insolvency in the insurance markets, but sharply disagreed as to the cause of the market pressures on insurers. Witnesses and lawmakers stressed the need to expand data collection efforts within insurance markets.

OPENING STATEMENTS

Chair Sheldon Whitehouse (D-RI) (statement) called attention to the impacts of climate change on insurance markets, and noted that it could impact the broader economy. He noted that insurance providers are a critically important component of the housing market: buyers may be hesitant to purchase property in a state where providers are not renewing policies or are pulling out altogether. Chair Whitehouse warned that state-backed insurers of last resort may not be solvent, and that small insurers may not have the resources to pay claims, pointing to Florida as an example of a state where these trends are already in place. He warned that in a state prone to heavy storms, large climate shocks can cause property damage at the same time that insurers become insolvent, increasing the likelihood of mortgage defaults. Finally, Chair Whitehouse concluded by expressing his fear of a spiraling financial crisis similar to that which took place in 2008.

Ranking Member Chuck Grassley (R-IA) (statement) disagreed with the need to focus on climate change, instead drawing attention to inflation and the national debt. He claimed that Democrats want insurers to "abandon" diversified portfolios, specifically fossil fuel projects. While he acknowledged that insurance premiums are high, he disagreed with the premise that climate change is a contributing cause.

WITNESS TESTIMONY

Commissioner Glen Mulready (testimony), of the Oklahoma Insurance Department, noted that convective storms and wildfires make up an increasing cause of property damage, broadening risks beyond earthquakes, hurricanes, and floods. He acknowledged that inflation has contributed to increased insurance rates. He encouraged homeowners to invest in proactive measures such as storm shutters, brush removal, and fire-resistant materials. Mr. Mulready relayed his belief that free-market competition is key to reducing costs, and warned that state-level policies regulating insurance rates will only cause insurers to leave markets entirely.

Mr. Rade Musulin (testimony) of Finity Consulting, noted that many states effectively subsidize the insurance of high-risk areas through pool programs like the Florida Hurricane Catastrophe Fund and Citizen's Property Insurance Corporation, which further contribute to rapid development in high-risk areas. He warned that if a large hurricane were to hit a major urban center in the state, it could exceed the system's capacity. He advised that building codes and land-use policies must be updated to address increased risk.

Dr. Ishita Sen (testimony), Assistant Professor of Finance at Harvard Business School, warned of the risks to financial and fiscal health posed by low-quality, questionably solvent insurers taking increasing portions of market share in states such as Florida. She further implied that the Government Sponsored Enterprises' (GSE) insurer requirements are "miscalibrated," and that many financial stability ratings are inflated.

Ms. Deborah Wood (testimony), A Florida resident, shared that Florida's insurance market is increasingly unaffordable for homeowners.

Dr. E.J. Antoni (testimony), of the Heritage Foundation, drew attention to increases in construction costs for single-family homes. He noted the need for insurers to remain solvent and disagreed that climate change has been a significant contributor to increased insurance rates.

DISCUSSION AND QUESTIONS

Risks in the Insurance Market

- Chair Whitehouse asked how severe weather events in high-populated areas can increase pressure and exceed the capacity of the insurance markets. Mr. Musulin noted that, in a scenario where a major hurricane hits central Florida, the state would need to find additional sources of funding — whether by raising assessment caps, or through other means.
- Chair Whitehouse questioned what broader risks are posed to the financial system by insurance markets. Mr. Musulin relayed that high growth and wealth accumulation have been concentrated in high-risk areas, many of which do not have building codes sufficient to withstand a major weather event. This could cause a domino effect if insurers cannot pay claims, he stated.

- Chair Whitehouse expressed concerns that Demotech insurance transfers risk and exposure from the state level to the federal government. Dr. Sen agreed, noting that "inflated" financial stability ratings could generate an excessive amount of high-risk mortgages backed by low-quality insurers. She elaborated that, if large losses are incurred, they will have to be covered by taxpayers. This would also impact the prices of mortgage-backed securities, she added. Dr. Sen further noted that insurers are major investors across asset classes, and they may have to offload securities at inopportune times.
- **Sen. Tim Kaine (D-VA)** called attention to high insurance rates on multi-family housing, and questioned if these markets are subject to similar dynamics as insurance for single-family homes. Dr. Sen confirmed that similar forces operate in both markets, and many insurance providers are active in both. However, she warned that the available data on multi-family housing insurance markets is not granular enough to make an accurate systematic analysis. She called for more robust data collection in this sector, arguing that risk-based capital requirements must be updated to account for modern wildfire and hurricane risks.
- **Sen. Jeff Merkley (D-OR)** expressed fear regarding growing wildfire risks across much of the U.S., noting that this has significantly broadened and deepened risks. He questioned what policies should be put into place to ensure that homeowners can continue to secure insurance and maintain their mortgages. Dr. Sen explained that there is not sufficient data on even defining the scope of the problem. Sen. Merkley reiterated the importance of countering and mitigating the impacts of climate change.
- Sen. Merkley noted that state-backed insurance programs have the potential to incur massive debts. Dr. Sen concurred and noted that while states generally have better capacity to withstand a significant loss, there will likely be major fiscal challenges for municipalities and state governments.
- **Sen. Ben Ray Luján (D-NM)** warned of increasing wildfire risks, especially across the western U.S. and noted that electrical providers are facing increased difficulty in obtaining wildfire insurance. In acknowledging the importance of hardening the electric grid, Mr. Musulin pointed out that doing so presents a simultaneous opportunity to modernize the grid to prepare it for a transition to renewable energy.
- Sen. Luján noted challenges in rebuilding smaller, rural communities impacted by wildfires or other natural disasters. Dr. Sen communicated that securing adequate homeowner's insurance is a major challenge in these situations, and the costs are extremely high.

Insurer Pressures

- Ranking Member Grassley and Dr. Antoni shared their belief that climate change is not a major contributor to insurance costs. They agreed that inflation is a key problem and called for balanced budgets.
- **Sen. Ron Johnson (R-WI)** claimed that inflation, the 2020 protest movement, overregulation, and the concentration of development in high-risk areas are responsible for increased insurance rates, rather than climate change. Dr. Antoni agreed, claiming that these factors account for "90 percent" of the increase in insurance costs.
- **Sen. Chris Van Hollen (D-MD)** noted the importance of collecting more detailed data on insurance markets to more thoroughly understand pressure on insurers. Dr. Sen reiterated

the importance of this point, noting the necessity of this data for both regulators and insurers. Mr. Mulready stated that an initial effort on data sharing has begun.

Market Policy Changes

- Responding to a question from Ranking Member Grassley ways to encourage competition in insurance markets, Mr. Mulready called for increased licensing and a "business-friendly environment." He reiterated his calls for homeowners to invest in mitigation and resilience.
- Mr. Musulin, in conversation with Sen. Van Hollen, reiterated the importance of updating land-use and building code policies.
- Sen. Romney expressed his belief that insurance policies encourage development in high-risk areas, and called for increased funding for mitigation efforts. The witness panel unanimously agreed. Mr. Musulin further called for updates to building codes. Dr. Sen noted that past inflationary cycles have not had similar impacts on home insurance markets. Mr. Mulready emphasized the importance of updating zoning to account for modern understandings of climate risks. Dr. Antoni emphasized the importance of investments in the maintenance of public infrastructure.
- Sen. Romney relayed his support for a global carbon tax.
- Sen. Luján questioned if the Federal Emergency Management Agency (FEMA) has adequate resources for rebuilding efforts. While he did not answer the question directly, Mr. Mulready offered a dialogue as to why investing in FEMA provides value to communities.