

DFS Issues Final Insurance Climate Change Guidance

November 17, 2021

The New York Department of Financial Services (the “DFS”) issued final guidance (the “Guidance”)¹ on November 15, 2021 that lays out a roadmap for how New York domestic insurers (“NY Insurers”) should manage the financial risks of climate change and describes the DFS’s expectations for NY Insurers in this regard, following up on a circular letter,² proposed guidance (the “Proposed Guidance”)³ and an analysis⁴ issued by the DFS since September 2020.

State insurance regulators, including the DFS, have increased their emphasis on the need for insurers to consider climate risks in recent years. The National Association of Commissioners (the “NAIC”) elevated state regulators’ work on climate and resiliency from a working group to a task force that reports to the NAIC’s Executive Committee. State insurance regulators also have worked independently or in partnerships with other regulators, legislators and interested parties. Before issuing the Guidance, the DFS (which regulates banking, insurance, and other financial institutions) announced the creation of a new Climate Division, promoting Dr. Yue (Nina) Chen from Director of Sustainability and Climate Initiatives to Executive Deputy Superintendent leading the new Division,⁵ indicating the DFS’s intention to be a leader in this area. As more states make increasing use of the annual NAIC Insurer Climate Risk Disclosure Data Survey, it is reasonably likely that other states, like New York, will begin requiring insurers to incorporate climate change risks into their governance and risk management processes.

The Guidance reflects industry commentary on the Proposed Guidance, which called for the addition of materiality standards, a response to the existing uncertainty and evolving nature of climate change risks, permission to incorporate climate change risk

¹ DFS Guidance for New York Domestic Insurers on Managing the Financial Risks from Climate Change, dated November 15, 2021, *available* [here](#). See also, the DFS’s announcement [here](#).

² For further information on Circular Letter Number 15, issued September 22, 2020, please see our previous client alert [here](#).

³ For further information on the Proposed Guidance, issued March 25, 2021, please see our previous client alert [here](#).

⁴ For further information on the Analysis, issued July, 2021, please see our previous client alert [here](#).

⁵ See DFS’s November 3, 2021 press release [here](#).

management into existing risk management frameworks, and a timeline for implementation.

Climate Change Guidance. As set forth in the newly issued Guidance, the DFS expects NY Insurers to manage the financial risks and take advantage of the opportunities arising from climate change. The Guidance sets forth the following expectations of NY Insurers.

- *Governance:* The DFS expects NY Insurers to integrate climate risk considerations into governance structures at the board and senior management levels. The Guidance reflects industry requests to permit governance of climate change risk matters at either the group or NY Insurer level and to provide room for discretion on materiality determinations by individual NY Insurers.
- *Risk Management Decision-Making Processes:* The DFS expects each insurer to document how its analysis and stress testing with respect to climate change is integrated into its business strategy, risk appetite framework and risk management and compliance processes, including enterprise risk management (“ERM”) functions. The Guidance reflects industry comments to allow for incorporation of climate change risks into existing risk management frameworks.
- *Scenario Analysis:* Each insurer will be expected to use forward-looking scenario analysis and stress testing to inform its identification and management of climate-related risks. The scenario analysis should cover the impact of climate-related physical and transition risks in the short, medium and long term. The Guidance reflects industry comments regarding materiality, only requiring such analysis if the insurer determines climate change risks are material, as well as comments regarding uncertainty, acknowledging that analyses should be used to understand potential risks rather than to dictate precise responses.
- *Disclosure:* Each insurer should enhance the transparency of its integration of climate risks into its governance and risk management. The Guidance responded to requests for clearer guidance on disclosure expectations, noting that the NAIC Insurer Climate Risk Disclosure Data Survey is acceptable if responses satisfy the requirements of the Guidance, permitting disclosure at the group level if the disclosure addresses practices at the insurer level and acknowledging that the substance and nature of disclosures may develop over the next two or three years.

Uncertainties, Timelines and Supervisory Dialogue. The Guidance acknowledges the uncertainties in climate change analysis and the need for a proportionate, progressive approach. The DFS expects the Guidance to serve as a basis for supervisory dialogue, with active supervision and enforcement to follow, after the industry and the DFS have

had an opportunity to implement the Guidance and other evolving practices in the industry and supervisory community. The Guidance also sets out specific timelines for implementing its various expectations, permitting implementation over the next two or three years. The DFS set an August 15, 2022 deadline for NY Insurers to meet the DFS's expectations regarding board governance and to have specific plans in place to address the DFS's expectations regarding organizational structure.⁶ DFS representatives also have stated that during the DFS's examinations, the DFS will consider NY Insurers' progress on evaluating and addressing climate risks.

The DFS has scheduled a webinar on November 22, 2021 to provide an overview of the Guidance.

We expect that incorporation of the Guidance into decision-making processes and compliance regimes will require a significant amount of industry attention over the next few months, and we would be happy to consult on any of these issues.

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Please do not hesitate to contact us with any questions.



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⁶ See Guidance at § 3.5.