

Remarks by Acting Assistant Secretary for Financial Institutions Laurie Schaffer at The Geneva Association's Programme on Regulation and Supervision (PROGRES) Seminar 2024

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INTRODUCTION

Good morning. Thank you to the Geneva Association for having me here today. I appreciate that many of you have traveled to Washington to participate in these important conversations about the insurance sector.

As the Acting Assistant Secretary for Financial Institutions, I oversee a broad policy portfolio at the U.S. Treasury Department, encompassing banks, credit unions, and the insurance sector, as well as cybersecurity and critical infrastructure, community development, and consumer protection. As we face increasing challenges domestically and internationally from the climate crisis and cyber events, our insurance work has often been among the top priorities across my portfolio in recent months.

Today I'm happy to discuss our work.

TREASURY'S ROLE THROUGH FIO IN MONITORING THE INSURANCE INDUSTRY AND INTERNATIONAL ENGAGEMENT

First, let me provide some brief background on the Federal Insurance Office at the U.S. Department of the Treasury. FIO was created in the wake of the 2008 financial crisis by the Dodd-Frank Wall Street Reform and Consumer Protection Act, which gave FIO the authority to monitor all aspects of the insurance industry. FIO is also authorized to collect and disseminate data and information on and from the insurance industry, serves as a member of the Financial Stability Oversight Council, assists the Secretary with the administration of the Terrorism Risk Insurance Program, and monitors the extent to which traditionally underserved communities and consumers have access to affordable non-health insurance products.

Internationally, FIO represents the United States on prudential aspects of international insurance matters, including serving as a member of the Executive Committee at the International Association of Insurance Supervisors (IAIS), and is authorized, jointly with the Office of the United States Trade Representative, to negotiate “covered agreements” concerning insurance or reinsurance prudential measures with foreign governments, authorities, or regulatory entities.

THE FEDERAL INSURANCE OFFICE’S WORK ON CLIMATE-RELATED RISKS AND INSURANCE

Let me start by talking about the ongoing work of Treasury and FIO to address climate risk in the insurance sector, which is affecting Americans across the country as many consumers face increased challenges finding available and affordable property insurance.

Since the beginning of this Administration, President Biden and Vice President Harris have been concerned with the significant impacts that climate change can have on American families, consumers, the housing market, and the broader economy. To address these impacts, the President issued an Executive Order in May 2021, which leverages a whole-of-government approach to climate-related financial risk. Treasury has played a critical role in the Administration’s effort.

In the Executive Order, President Biden tasked FIO to: (1) “assess climate-related issues or gaps in the supervision and regulation of insurers” and (2) “further assess, in consultation with States, the potential for major disruptions of private insurance coverage in regions of the country particularly vulnerable to climate change impacts.”

In 2023, as part of these efforts, FIO issued a report on Insurance Supervision and Regulation of Climate-Related Risks highlighting the initial efforts of state regulators and the National Association of Insurance Commissioners (NAIC) on this topic. The report provides 20 recommendations for ways that state efforts could be expanded, focused, and, where appropriate, made more uniform among the states. This report provides a high-level framework outlining how states can make progress in the important area of addressing climate-related risks faced by insurers and consumers.

Treasury and FIO also remain focused on our efforts to analyze ZIP Code level homeowners’ insurance data to help improve our understanding of the impacts of climate-related financial risks on the insurance sector. The market challenges presented by climate change are significant, and in many locations, it is increasingly difficult for homeowners and consumers to find and afford insurance. The average homeowner’s insurance premiums have increased by almost 20 percent between 2021 and 2023, with projections of more double digit increases in some states this year. In addition, some insurers are no longer writing new business in or withdrawing completely from a number of areas

that face a range of climate risks. The number of policies issued by residual market insurers, which are insurers of last resort in 32 states and the District of Columbia, has almost doubled, from 1.38 million in 2019 to about 2.71 million in 2023.

To better understand these and other issues facing U.S. homeowners, on March 8 of this year, FIO announced the launch of a first-of-its-kind collaboration with the NAIC and state insurance regulators to collect ZIP Code level homeowners' insurance data from the largest homeowners' insurers across the country. Treasury and FIO coordinated extensively with state insurance regulators and the NAIC on a single data collection that meets our complementary but distinct needs. This partnership on data collection is an important initiative for the American public, insurers, and state regulators, as well as for FIO and the NAIC.

FIO will use this data to conduct a nationwide assessment of climate-related financial risks to consumers across the United States for owner-occupied homeowners multi-peril insurance policies between 2018 and 2022. Specifically, FIO will use the data to calculate common insurance underwriting metrics on information such as average premiums, loss ratios, claims frequency, and non-renewal rates. These key metrics will be used to analyze trends over time across ZIP Codes facing varying levels of risk from climate-related events. As we continue to receive data from the NAIC, FIO expects to conduct and publish its analyses in a report issued by the end of the year.

FIO's climate work complements the efforts that states are undertaking to understand and address market challenges by adding a national perspective on the impact that climate change is having on homeowners. Our respective work at Treasury and at the state level is critically important to evaluating and understanding how increased stress in U.S. property insurance markets is affecting homeowners. We also see significant benefits to continuing data collection efforts and the FIO/NAIC partnership in future years – as we will also need updated and additional insurance data to help inform our work.

Detailed insight into insurance market challenges is particularly important at a time when the Biden-Harris Administration is implementing historic legislation to invest billions in strengthening the resilience of climate-vulnerable communities. This includes the Bipartisan Infrastructure Law and Inflation Reduction Act which dedicated more than \$50 billion to advance climate resilience strategies in every community in America. The National Initiative to Advance Building Codes further reinforces the Administration's efforts to meaningfully increase resilience to climate change.

As we move forward, we are committed to engagement and collaboration with stakeholders and the insurance industry, including those of you in this room.

Finally, I wanted to touch on another important area of climate work at Treasury relating to the interconnectedness of the housing and insurance markets.

The availability of insurance can have potentially significant consequences for homeowners and their property values, which if severe enough could spill over to other parts of our interconnected financial system. Financial institutions and investors hold assets such as mortgages and securities that are directly or indirectly affected by insurance coverage. Insurance policies may exclude coverage for specific perils; for example, most multi-peril home insurance policies do not cover flood damages. And some homeowners may choose to forego insurance coverage, including for reasons of affordability. Any resulting mortgage defaults by homeowners will push losses into other parts of the financial system.

The impact of escalating costs for insurance can be most acute for low-income households. One study finds that twelve percent of homeowners in the United States did not purchase homeowners' insurance; and about half of homeowners that did not purchase insurance had a household income of less than \$40,000 per year. In addition, the majority of low-income households are not homeowners themselves but may absorb the higher cost of property insurance through their rent. And, and after disasters, renters generally have less access to financial assistance as compared to homeowners, making recovery more difficult for these households.

The impact of insurance costs on housing affordability and availability is an important consideration that we will need to continue to study, particularly for vulnerable populations.

Our collective efforts in this area will only become more important in future years. We want to prioritize ensuring that insurance markets continue serving their role in the economy and that policymakers can help consumers and families take the necessary steps to help mitigate the impact of climate risks on their household finances.

FIO'S WORK ON INSURANCE AND CATASTROPHIC CYBER RISK, INCLUDING AS PART OF THE ADMINISTRATION'S NATIONAL CYBERSECURITY STRATEGY AND THE NEW FIO-NSF IUCRC

CATASTROPHIC CYBER RISK/ PUBLIC-PRIVATE RISK SHARING

Next, I want to discuss Treasury's work to examine a potential federal insurance response to catastrophic cyber risk.

Treasury and FIO have been working closely with our partners across the Administration, including the Cybersecurity and Infrastructure Security Agency at the Department of Homeland Security and the Office of the National Cyber Director at the White House, to examine potential forms of a federal insurance response to catastrophic cyber risk, including how insurance, if it is available, can mitigate the effects of a catastrophic cyber incident and protect our nation's economic resilience. Preparing for a catastrophic cyber incident is a proactive approach in line with Strategic Objective 3.6 in President Biden's 2023 National Cybersecurity Strategy, which states:

"In the event of a catastrophic cyber incident, the Federal Government could be called upon to stabilize the economy and aid recovery. Structuring that response before a catastrophic event occurs – rather than rushing to develop an aid package after the fact – could provide certainty to markets and make the nation more resilient."

The U.S. cyber insurance market has grown considerably in recent years and remains the largest in the world. These products primarily address attritional cyber losses, as opposed to catastrophic cyber incidents – the kind that could do systemic damage to the national economy. Insurance for attritional cyber incidents, such as most ransomware attacks, has expanded in recent years in response to the growing risk; however, the market has pulled back from covering catastrophic cyber incidents.

Accordingly, FIO's analysis is focusing on how a federal insurance response to catastrophic cyber risk can be cabined alongside the existing and expanding commercial cyber insurance market. As Treasury progresses in our work, we are assessing various approaches for sharing catastrophic cyber risk between the public and private sectors, as well as considering how they could foster greater resilience in our financial system, mitigate moral hazard, and protect taxpayer interests.

As part of our continuing efforts, FIO hosted a second stakeholder conference at Treasury in May, which launched the current phase of Treasury's work with discussions about potential forms a federal insurance response might take. FIO is working closely with Treasury's inter-agency partners on potential policy responses and will have further updates later this year.

The recent CrowdStrike incident highlights how impactful a cyber incident, even an accidental incident, can be across the economy and served to emphasize the importance of Treasury's cyber work. This was a wide scale global event that affected several critical infrastructure sectors including the financial, transportation, and healthcare sectors, among others. While this incident was widespread, it appears to be a loss that the insurance industry was prepared to respond to, rather than a catastrophic event, and it looks likely that it will not have a material effect on global insurer and reinsurer financial results.

Advance preparation for a response to catastrophic cyber incident, illustrated by FIO's ongoing work and other government initiatives, can help improve the U.S. economy's resiliency if and when a systemic cyber event occurs.

FIO-NSF IUCRC

I would also like to take a brief moment to discuss a new public-private partnership. This year, FIO initiated a collaboration with the National Science Foundation (NSF), insurance sector stakeholders, and the academic community to consider how to better predict and insure terrorism and catastrophic cyber risks through a new Industry-University Cooperative Research Center. The U.S. government has a long history of employing public-private collaborations to study critical challenges, and we welcome the academic and private sector's partnership with Treasury and the NSF in addressing the challenge of terrorism and catastrophic cyber risks.

This is the first time that Treasury has formally partnered with National Science Foundation, and we're excited about the potential benefits of the collaboration. Industry-University Cooperative Research Centers (IUCRCs) facilitate work between university academic teams and an industry consortium to carry out cutting-edge research focused on the collective needs of a sector of the U.S. economy.

This new center will stimulate research and develop potential solutions that provide insurers, government, and other stakeholders with additional data and improved modeling and underwriting tools, methodologies, and practices for insuring terrorism and catastrophic cyber risks. Through these efforts, the IUCRC could help strengthen the resilience of the U.S. economy by potentially expanding insurance coverage for these risks through improved insurance modeling and underwriting. The IUCRC's research may also help FIO's ongoing work assessing catastrophic cyber risk in the insurance sector and administering the Terrorism Risk Insurance Program.

FIO'S INTERNATIONAL WORK

Next, I'd like to provide an overview of some of our international work.

IFTRIP

I'll start by highlighting our work collaborating with international partners on terrorism risk. I would highlight Treasury's leadership role as chair of the International Forum of Terrorism Risk (Re)Insurance Pools (IFTRIP), which is a forum of 15 nations, including the United States, supporting

initiatives for closer international collaboration among sovereign-backed terrorism reinsurance pools. FIO hosted the IFRIP Annual Conference at Treasury in April.

Under U.S. leadership, we aim to increase IFTRIP's collaborative partnerships with other organizations, building upon the IFTRIP's prior work with the Geneva Association examining the insurability of hostile cyber activity. I'm pleased IFTRIP is now working with the Geneva Association, and many of you here today, on a further collaborative project that aims to assess shifts in the chemical, biological, radiological, and nuclear risk landscape, and the insurance response for those perils.

We are excited about the direction of IFTRIP's future work and look forward to building upon the prior IFTRIP accomplishments and expanding the goals of this organization.

INTERNATIONAL ASSOCIATION OF INSURANCE SUPERVISORS

FIO also continues to fulfill its statutory role representing the United States in the IAIS and in other forums on prudential international insurance measures. In this capacity, one of our top international priorities is engaging at the IAIS, along with our NAIC, state insurance regulators, and Federal Reserve Board colleagues, in key discussions around the Insurance Capital Standard (ICS). As many of you know, the ICS is scheduled to be adopted by the IAIS at year-end 2024. FIO is also focused on the ongoing work surrounding the comparability assessment of the Aggregation Method. The next few months will be a significant period of meetings, as the IAIS works toward the completion of these important initiatives. We look forward to our continued collaboration with IAIS members and our U.S. colleagues.

TREASURY'S WORK ON ARTIFICIAL INTELLIGENCE

Turning next to artificial intelligence (AI) and the financial services sector, the Biden-Harris Administration has been focused on harnessing AI's potential to fuel innovation while mitigating risks, as reflected in President Biden's landmark Executive Order on AI last year. Treasury, and my office, are playing a key role in spurring responsible innovation in relation to AI and financial institutions.

Under the President's Executive Order on AI, in March, Treasury released a detailed report providing an extensive overview of current use cases and best practices related to AI for cybersecurity and fraud prevention in the financial sector. In June, Treasury formally launched a Request for Information to

seek comments on the current uses, opportunities, and risks of AI in the financial services sector. We received over 100 comments and are in the process of reviewing these submissions.

I would also highlight that next week FIO will convene a roundtable on AI in the insurance sector to discuss the benefits and challenges associated with the use of AI by insurers, potential consumer protections to prevent discrimination, and the current state regulatory framework and best practices for the sector. We expect that this event and our other stakeholder engagement will assist FIO in better understanding this area, which is of such growing importance.

FIO'S WORK ON TITLE INSURANCE

In addition to the upcoming AI roundtable, FIO recently hosted a roundtable to discuss the title insurance industry and analyze potential reforms. FIO was tasked with convening the roundtable in connection with President Biden's call for federal agencies to take all available actions to lower home closing costs and help more Americans access homeownership. We look forward to continued engagement on these issues and support increased qualitative and quantitative analyses in this area to better assess how the title insurance industry is benefiting consumers and homeowners.

OCCIP'S WORK ON CYBERSECURITY, INFORMATION SHARING, AND INTERNATIONAL COOPERATION

I would also like to provide a brief overview of work that Treasury's Office of Cybersecurity and Critical Infrastructure Protection (OCCIP) is leading. Earlier this year, Treasury established Project Fortress, an initiative led by OCCIP to improve the security and resilience of the financial services sector through forward-leaning public-private information sharing mechanisms. Project Fortress includes a mix of proactive defensive and offensive measures to help secure the financial sector. The initiative represents a new model of proactive sector risk management, leveraging the vast amount of data and capabilities that exist across the federal government and the private sector.

Treasury is also making tremendous progress on the issue of cloud security. Together with the Financial Services Sector Coordinating Council, Treasury recently published a suite of resources for financial institutions on secure cloud adoption. To name a few, these include a common cloud lexicon for financial institutions and regulators, information sharing and coordination of examinations, and best practices for managing third-party risk associated with cloud outsourcing. This work is the culmination of an unprecedented public-private partnership known as the Cloud Executive Steering Group, consisting of sector CEOs and regulatory agency heads.

Treasury is continuing its push for technology modernization through OCCIP's international efforts, working with partners abroad to detect threats approaching their networks. Earlier this year, OCCIP organized and participated in the G7 Cyber Expert Group's Cross-Border Coordination Exercise. Treasury also signed a memorandum of understanding and cooperation (MoU) in cybersecurity with the National Bank of Ukraine, facilitating an ongoing exchange of information between the National Bank of Ukraine and Treasury. The MoU is part of a whole-of-government effort to support the people of Ukraine and helps Treasury stay ahead of risks to the U.S. financial services sector.

FINANCIAL INCLUSION

Before closing, I want to mention Treasury's work to develop a National Financial Inclusion Strategy. Treasury has met with organizations across the financial sector, as well as with fellow policy makers and community and consumer organizations, to discuss financial barriers faced by underserved communities.

The inaugural Strategy will be released later this year and is intended to further cross-sector efforts to reduce disparities and ensure that consumers, particularly those from underserved populations, have equitable access to financial information, products, and services. As all of you know, access to affordable insurance products can be an important way for consumers to build financial resilience and security.

CLOSING

Let me close by thanking you again for having me here to speak about the important work we are doing at Treasury related to climate, cyber risk, and in many other areas. I look forward to engaging with many of you as we tackle these and other challenges ahead.

I would be happy to take questions.



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