Floods, Fires and Droughts - Insurance in the Era of Climate Change, 35:5 Can. J. Ins. L. at 131 (September 2017)

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Introduction

The fires that ravaged Fort McMurray, Alberta in the summer of 2016 brought the issue of climate change back into the national spotlight. The insured losses stemming from the fires have been estimated at approximately $4 billion, which would constitute the greatest insured loss in Canadian history. As was the case with the Calgary floods in 2013, extreme weather events inevitably raise inevitable insurance coverage questions. By July 2016, approximately 45,000 claims had been tendered to insurers seeking coverage for fire losses. Personal and commercial insureds found themselves wondering whether their losses were covered.

Whether, and to what extent, climate change was a factor in the fires may be difficult to discern with scientific accuracy, but the fires brought to mind the impact climate change may have on the severity and number of catastrophic weather events in the future. Events such as the fires in Fort McMurray and the floods in Calgary are two among many stark reminders of the potential impact of climate change, which the scientific community now believes will cause a rise in global temperatures and exacerbate weather-related disasters. 2016's $210 billion in losses stemming from natural catastrophes was already one of the highest totals on record. Those in the insurance industry may not be surprised to hear that less than one-third, or approximately $50 billion, of these losses were insured.

This paper will analyze how climate change may impact insurance coverage, how insurers have responded to and are preparing for climate change. We will explore some of the initial climate change-related insurance litigation.

How Climate Change Might Impact Insurance Claims

Weather events are perhaps the greatest catalyst of insurance claims. If scientists are correct and climate change continues to raise global temperatures, more severe and unpredictable weather events are likely to have a radical impact on the number and type of claims under a number of coverages.

Property Insurance

Property insurance is likely to be the greatest source of exposure from climate change. Property insurance has been at the forefront of industry concerns regarding climate change. In one survey of executives and managers at small and medium-sized businesses in thirteen countries, approximately one-third of respondents stated that material damage was likely to be the most severe risk to their business due to climate change.

As climate change progresses and its effects become increasingly clear in the form of extreme weather events, insurers will be called upon to respond to an increase in the number of property claims. The Fort McMurray fires, for example, brought some insurers a decade worth of claims in the span of several months. As larger floods, faster-spreading fires and stronger winds wreak havoc across Canada, property insurers will be called upon for indemnity. Insurers, in turn, are likely to review their underwriting and policy wordings and premiums charged on property policies.

Business Interruption

Business interruption coverages will also be particularly susceptible to climate change. The study referenced above revealed that downpours, heavy rain, droughts and severe heat were the natural events believed to have the most potential to hurt businesses. The second greatest climate change-related risk was revealed to be business interruption threats. Of course, the former will act as a catalyst for the latter. Disruptions in supply chains, transportation, utility services and communications networks caused by extreme weather events will aggravate what might have otherwise been simple and localized claims.

In the era of climate change, businesses may find themselves being sued for failing to have implemented appropriate climate change contingency plans for losses arising from delays in restoring operations following weather events. There are several less obvious consequences of climate change that could increase business interruption risks and claims, such as higher energy and clean water costs and the health effects of extreme weather on employees.

Environmental Liability

One obvious area of insurance that is likely to be transformed by climate change is environmental liability. Consideration of the 2010 Deepwater Horizon oil spill is illustrative. A similar incident occurring in 2100 might be exaggerated, for example, by violent ocean storms which make cleaning and rescue operations more difficult. Meanwhile, stronger winds might spread contaminants, making relief operations more difficult. Higher temperatures might place added strain on response crews operating for long periods and may even increase the risk of the contaminant igniting, further complicating operations.

While large-scale environmental disasters are among the most obvious examples of how climate change might impact environmental liability, extreme weather events will also exacerbate environmental claims at the regional and local level. If temperatures rise as expected, businesses operating in small towns that handle dangerous chemicals or gases might be subject to a greater risk that harmful vapours will spread or combust. If climate change results in stronger and unpredictable wind-related events, coastal businesses may be subject to a greater risk of polluting waters.

Personal Injury & Municipal Liability

At an even more localized level, climate change is likely to increase the number and severity of personal injury claims. In particular, climate change is expected to have a substantial impact on automobile-related claims, as more frequent extreme weather events will disrupt driving conditions. Videos of Fort McMurray fires creeping up to the sides of Alberta's highways are an alarming example of how climate change-related weather events may transform a morning commute into a health and driving hazard.

An increase in slip and fall incidents caused by severe rain, snow and heat-related collapses is likely to spur insurance claims. Concomitantly, municipal liability insurers should anticipate occupier liability claims. However, municipal insurers may face more obscure claims related to their negligence in zoning and planning, given that extreme weather events will cause unpredictable flooding and ice hazards. One can envisage insureds making courtroom arguments that their home would not have been destroyed if their municipality had not allowed private residences to be built so close together, allowing fires to spread between buildings.

Professional Errors & Omissions

More professional E&O claims can be expected as the effects of climate change become increasingly realized. Engineers and architects are and will be expected to design and build living spaces and office towers that will withstand increasingly severe weather. Those that fail to account for climate change may find themselves subject to claims. Given the unpredictability of climate change, insurers may revise their E&O policies to limit duty to defend and indemnity obligations for such claims.

Product Liability

Finally, we anticipate that product liability claims will proliferate as businesses fail to redesign their products to make them suitable for extreme weather. For example, sustained increases (or decreases) in temperature could foreseeably impact the effectiveness of certain concretes, steels or other building materials used in homes and office towers and subsequent failures could lead to claims. Similarly, building foundations damaged from an increased exposure to water from rain and flooding and damaged window shutters resulting from strong wind gusts may lead to product liability claims.

Insurers Respond to Climate Change

While many industries have been slow to accept climate change as a real or serious issue, or have failed to anticipate the consequences it may have on their operations, the insurance industry has instead been a leader in this regard. Munich Re is reported to have first raised caution regarding global warming in 1973, remarking at that time how damage and loss caused by flooding was increasing. Many years before the 1992 Rio Earth Summit, insurance industry leaders had already recognized that claims were outpacing risk tables and models.

Insurers have begun to respond to climate change in a number of ways. In 2016, Swiss Re announced that it would be adopting climate-related financial disclosure recommendations that had been created by the Task Force on Climate-Related Financial Disclosures. As a result, Swiss Re has agreed to alter its risk analysis to include in future annual financial reports:

- losses that can be expected from weather-related catastrophes;
- a “description of physical risks from changing frequencies and intensities of weather-related perils”; and
- how a “2°C scenario” may impact its business strategy and financial planning.

Intact has sponsored the Intact Centre on Climate Adaptation (ICCA), a Canadian applied research centre that focuses on mobilizing practical and cost-effective solutions to address climate change and extreme weather events. The ICCA also operates as an incubator of new adaptation ideas, conducting research, knowledge mobilization and promoting initiatives aimed at removing some of the risk and negative impact which has or will result from climate change and extreme weather events. In November 2015, Intact announced a gift of $4.25 million directed in support of the ICCA mission and goals.

Canada’s insurance industry has also in recent years shifted its focus towards “de-risking” insured properties to respond to climate change as its effects begin to manifest. Strategies are being passed on to homeowners, for example, who are being encouraged to adopt procedures that will reduce the risk of property damage, such as by directing runoff water away from their homes, installing devices that operate to prevent sewer backup, by covering window wells to prevent basement flooding, or by installing measures to render their living spaces (more) fireproof. While Canadians may be slow to adopt such measures, the implementation of these and similar practices will work towards reducing risk for insureds and insurers.

Climate Change Litigation

Climate change litigation has emerged in the United States. In the “Comer”[1] litigation, residents and landowners on the Mississippi Gulf Coast filed a class action complaint seeking damages caused by “global warming”. The litigation was brought against dozens of the largest American companies in the energy and chemical industries. The plaintiffs claimed that the defendants’ operations and emission of harmful gases contributed to global warming and corresponding increases in surface, air, and water temperatures. It was alleged that same subsequently contributed to the strength of Hurricane Katrina and the widespread property damage it caused. Damages were sought under various heads.

The Comer litigation was unwieldy. At trial, the case was dismissed without a written opinion, with the Court noting that the climate change debate did not have a place in the courtroom prior to the implementation of legislation outlining appropriate standards to measure conduct. The Fifth Circuit Court of Appeals held that the plaintiffs’ injury claims were traceable to the defendants’ conduct and, accordingly, found that the plaintiffs had standing to advance claims of nuisance, trespass, and negligence. However, this finding was vacated and the Supreme Court of the United States denied the plaintiff’s subsequent petition for a writ of mandamus. Subsequent related “Comer II” litigation by the plaintiffs was unsuccessful on a number of grounds.

In Native Village of Kivalina v. ExxonMobil Corp.[2] an Alaskan village sued energy utilities, oil companies and a coal company. The plaintiffs asserted that the defendants were responsible for excess emissions of greenhouse gases which contributed to global warming and resulted in the slowed formation and expedited melting of arctic sea ice. This was alleged to have, in turn, expedited erosion caused by winter storms. The plaintiffs sought redress in the form of the costs of relocating their village. The Ninth Circuit Court of Appeals reviewed the American common law of nuisance and the doctrine of displacement and held that: “under current Supreme Court jurisprudence, if a cause of action is displaced, displacement is extended to all remedies” and that “Congressional action, not executive action, is the touchstone of displacement analysis.”

The Comer and Kivalina litigation imply that until governments enact legislation containing standards to measure conduct and statutory causes of action, climate change lawsuits are unlikely to be successful.

Climate Change Insurance Coverage Litigation

As climate change litigation becomes more common, corresponding coverage litigation will necessarily follow. The limited but emerging body of climate change litigation has demonstrated how issues of standing, proximity, causation and public policy are crucial in respect of the success of such claims and plaintiffs have been largely unsuccessful to date. However, whereas climate change litigation involves such preliminary legal issues that have impeded plaintiffs in their pursuits, we anticipate that climate change coverage litigation will continue to be subject to traditional insurance law principles.

This was the case in AES Corp. v. Steadfast Insurance Co.[3], which was duty to defend litigation related to the Kivalina case discussed above. Steadfast had issued a series of CGL policies to AES Corporation, who had been named as a defendant in the underlying litigation. The allegations against AES were that it intentionally emitted greenhouse gases and knew or should have known of the impacts of its activities. AES was alleged to have intentionally and negligently violated federal and state laws. AES requested that Steadfast provide it with a defense pursuant to its CGL policies. Steadfast provided a defense under a reservation of rights and subsequently filed a duty to defend application. At trial, it was held that "Steadfast ha[d] no duty to defend AES in connection with the underlying Kivalina litigation because no "occurrence" as defined in the policies ha[d] been alleged in the underlying Complaint."

The Virginia Supreme Court granted discretionary review. Steadfast argued that "occurrence" was defined as an "accident" and that Kivalina's complaint alleged intentional conduct with known consequences. AES asserted that the Village's alternative allegation, that AES intentionally emitted greenhouse gases, but only "knew or should have known" the consequences of its action, described an "accident". AES argued that because the Village did not argue that the harm was solely a direct and certain consequence of these acts, the allegations constituted an "accident". In the first of two decisions, the Court held that Steadfast did not have a duty to defend on the basis that "[w]hen the insured knows or should have known of the consequences of his actions, there is no occurrence and therefore no coverage." On a rehearing, the Court held that as the Village had alleged that the harm caused by AES's intentional acts was not simply foreseeable but instead a "natural or probable consequence" of the acts, the resulting alleged injury was not an "accident". Accordingly, there was no "occurrence" and no duty to defend.

Novel Issues in Climate Change Insurance Litigation

While climate change litigation remains in its infancy, there have been a number of cases which illustrate how insurance can come into play in these cases.

iMatter Utah v. Njord[4] arose out of permit problems encountered by two groups, who wished to march down a street in Salt Lake City to raise awareness about climate change. The Utah Department of Transportation (UDOT) required the two groups, iMatter Utah and Positive Change Utah, to obtain insurance for the events and to sign an indemnification form that would protect UDOT and the State of Utah from liability for certain actions that might occur during the march. The members of the climate change groups argued that the insurance and indemnification requirements were unconstitutional as the provisions burdened the exercise of the Plaintiffs' rights under the First Amendment of the United States Constitution. UDOT responded that the requirements were content-neutral time, place, and manner restrictions which did not impermissibly restrict the plaintiffs' speech. The United States District Court, District of Utah, Central Division found that the insurance and indemnification requirements were not constitutionally sound and should not be enforced against the Plaintiffs.

The plaintiff in re Fairway Grp. Holdings Corp. Sec. Litig.[5] alleged that the defendants made material misstatements and omissions in order to make Fairway Group Holdings Corp.'s initial public offering more attractive to investors. Notably, a "Risk Factors" section of the IPO prospectus and June 6, 2013 10–K contained a subheading titled "Severe weather, natural disasters and adverse climate changes may materially adversely affect our financial condition and results of operations." In Fairway's August 2013 10–Q, the "Effect of Hurricane Sandy" was listed under the heading "Factors Affecting Our Operating Results." That subheading discussed store closures and damage, as well as insurance claims and premiums. Of relevance, the United States District Court for the Southern District of New York found that it was not clear how a reasonable investor would read these statements as implying that future sales at existing locations would be greater than they were in 2012, or how they were rendered materially misleading by omission of the fact that sales spiked before and after Hurricane Sandy.

Finally, in National Wildlife Federation v. Federal Emergency Management Agency[6], National Wildlife Federation ("NWF") brought a suit against the Federal Emergency Management Agency ("FEMA") for violations of the Endangered Species Act in its implementation of the National Flood Insurance Program ("NFIP"). Under The National Flood Insurance Act ("NFIA"), FEMA must provide flood insurance to communities which have, inter alia, "evidenced a positive interest in securing flood insurance coverage under the flood insurance program". Further, the Endangered Species Act ("ESA") required federal agencies to "ensure" that their actions did not cause "jeopardy" to endangered or threatened species. In the event that they did, the appropriate service, in this case National Marine Fisheries Service ("NMFS"), is required to issue a biological opinion detailing how the proposed action "affects the species or its critical habitat." If a species might be endangered by the agency action, the service suggests a "reasonable and prudent alternative" ("RPA") to the agency's proposal.

In 2003, NWF brought suit alleging that FEMA was in violation of the Endangered Species Act for failing to comply with its procedural obligation to consult with the NMFS on impacts of the NFIP to the Puget Sound Chinook salmon, a threatened species. NMFS presented FEMA in 2008 with an RPA to the NFIP. NWF identified two primary concerns with FEMA's compliance. NWF contended, inter alia, that FEMA had failed to update its maps for accuracy and to account for future climate change and failed to offer useful guidance on mapping for future climate change. While the holding of the United States District Court Western District of Washington is not particularly relevant for present purposes, it illustrates how legislative mandates, insurance regimes and climate change can interact to create novel causes of action.

Conclusion

While the effects of climate change are only beginning to be understood, it is possible to forecast the impact it may have on the insurance industry. As weather becomes increasingly severe, more and novel claims are to be expected under most types of policies. The litigation which stems from these claims will encourage nuanced and complex arguments, defences and proposed causes of action. The insurance industry will be watching closely as governments

introduce climate change legislation and regulations that contain behavioural standards, causes of action and insurance requirements.

Much less is certain on the insurance underwriting side. Some have predicted that premiums will rise as insurers are summoned to respond to larger than expected losses. Conversely, losses stemming from certain coverages may be rendered too costly and insurers may cease to underwrite certain exposures. This could create new opportunities for alternative insurance. Indeed, while climate change is expected to be a disruptive influence on the insurance industry in the coming decades, it may also provide opportunities to insurers and counsel.

[1] See, for example, *Comer v. Murphy Oil USA*, 607 F.3d 1049 (5th Cir.2010).

[2] *Native Vill. of Kivalina v. ExxonMobil Corp.*, 696 F.3d 849, 867 (9th Cir.2012).

[3] *AES Corp. v. Steadfast Ins. Co.*, 725 S.E.2d 532 (Va. 2012).

[4] *iMatter Utah v. Njord*, 980 F. Supp. 2d 1356, 1370 (D. Utah 2013), aff'd, 774 F.3d 1258 (10th Cir. 2014).

[5] *re Fairway Grp. Holdings Corp. Sec. Litig.*, No. 14-cv-00950, 2015 WL 4931357, at *20 (S.D.N.Y. Aug. 19, 2015).

[6] *National Wildlife Federation v. Federal Emergency Management Agency*, 2014 WL 5449859 (W.D. Wash. 2014).