Business Insurance

Risk Management

Directors may feel the heat on climate issues

Judy Greenwald

8/7/2017

Climate change is not yet a major issue for directors and officers, but experts expect it to become one.

The most significant portent of this may be a climate change resolution approved by a majority of Irving, Texas-based Exxon Mobil Corp. shareholders earlier this year over the firm's opposition. A putative class action securities lawsuit has also been filed against the company over the issue.

Despite President Donald Trump's recent withdrawal from the Paris climate accord, the issue is widely expected to demand more of directors and officers' attention. This will be particularly true for companies that leave "carbon footprints," including oil and gas companies, coal companies, utilities, auto manufacturers and transportation firms.

But policyholders of all types also may be vulnerable to catastrophic damage to their properties that is the result of climate change, say observers. The issue also has a potentially significant impact for insurers in terms of their exposure to catastrophe-related claims and their own investment portfolios, experts say.

In addition to withdrawing from the Paris climate accord, President Trump, who has disparaged the concept of climate change, signed an executive order in March that seeks to curb the federal government's enforcement of climate change regulations. But experts expect any regulatory vacuum to be filled by other regulators, particularly state attorneys general.

Experts say there would be coverage under company D&O liability policies for securities class action litigation.

“When you combine the political motivations of the institutional investors and the (nongovernmental organizations) and the litigation incentives of the plaintiff lawyers … there’s an opportunity for this to become more of an issue than it is now,” said Kevin LaCroix, executive vice president of RT ProExec, a division of R-T Specialty L.L.C., in Beachwood, Ohio.

The most likely exposures are going to be disclosure-based claims, with allegations directors “did not disclose the likely impact of carbon emissions or climate change issues on the company’s operation and profitability,” said Dan A. Bailey, a member of Bailey Cavalieri L.L.C. in Columbus, Ohio.

For example, if a hurricane leads to unprecedented flooding that damages physical plants, causing a financial impact, questions will arise as to “how well could these have been foreseen, what disclosures should have been made,” said Joseph Monteleone, senior counsel with Rivkin Radler L.L.P. in Hackensack, New Jersey.

Meanwhile, increased activity by nonfederal regulators “could get messy” for policyholders, said Rob Yellen, New York-based executive vice president of Willis Towers Watson P.L.C.’s FINEX North America. “States have their own environmental laws and they have their own environmental organizations,” which means policyholders could find themselves fighting battles in many places as a situation moves away from strong central mechanisms, Mr. Yellen said.

The issue could affect insurers directly, experts say. “If climate change produces more extreme weather events, it could have significant implications for property insurers,” said Mr. LaCroix.

The Kansas City, Missouri-based National Association of Insurance Commissioners “has been very active in encouraging insurance companies to be more proactive in describing the impact on their financial health and performance from extreme weather events caused by climate change,” he said.

Key Coleman, a Philadelphia-based director with accounting and advisory firm Marcum L.L.P., said the NAIC push in this area was initiated by the California Insurance Department when Insurance Commissioner Dave Jones requested not only that insurers disclose their carbon-associated investments, but also asked them to divest their coal investments.

“That was like a line in the sand,” which was adopted by six states, Mr. Coleman said: California, Connecticut, Montana, New Mexico, New York and Washington.

Meanwhile, 12 Republican attorneys general and Kentucky Gov. Matt Bevin sent a letter to Mr. Jones in June threatening legal action over the intiative, calling it “misguided.”

Climate-related shareholder litigation is likely to be covered by D&O insurance, say experts. “In many ways, it’s a very conventional securities class action lawsuit,” said Mr. LaCroix.

“I’d say that most companies have modified their D&O policy forms to ensure that coverage is clear in the event of such shareholder suits, notwithstanding the standard pollution exclusion language,” said Peter M. Gillon, a partner with Pillsbury Winthrop Shaw Pittman L.L.P. in Washington. “To the extent a company has not made those modifications on their policies, they should be looking at that seriously now.”

Referring to regulatory investigations, Sarah Downey, New York-based U.S. D&O product leader for Marsh L.L.C., said some policies provide broader preclaim inquiry coverage, but “that isn’t always a given. You have to negotiate for it.”