

Adaptation Case Study #4: The Co-operators

SECTOR: INSURANCE

Location: Guelph, Ontario



Natural Resources Canada
Ressources naturelles Canada

Canada



Network for
Business Sustainability

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Introduction

In 2013, Alberta, Canada, experienced heavy rainfall that triggered the most catastrophic flooding in Alberta's history. The total damage estimates exceeded \$7 billion, most of which was not covered by insurance.¹ The federal government, through the federal disaster recovery program, covered the largest part of the bill.

Canadian insurer The Co-operators knew that climate change was likely to produce more extreme weather events, and wanted to be part of the solution.

“From a societal perspective, in Canada we are managing by disaster when it comes to climate change adaptation,” said Rob Wesseling, executive vice-president and chief operating officer, Property and Casualty Operations and The Sovereign General Insurance Company.

“We’ve seen wildfires in Slave Lake, we’ve seen flooding and extensive damage in Calgary and Toronto. We see the impact of ice storms. So we’re right out there on the front lines paying claims and helping people live with the damage that’s being caused by climate change.”

Bruce West, CPA, CA, executive vice-president and chief financial officer

“There is a significant effort focused on mitigation but there is limited activity associated to adaptation, and when we do tend to focus on it, it tends to be after a disaster.” Prevention is key, said Wesseling: “A billion-dollar infrastructure project makes sense in the context of an event that, should it occur, would cost \$5 billion.”

Bruce West, CPA, CA, executive vice-president and chief financial officer, explained the intersection with The Co-operators vision: “We are on the front-line of climate change. Our vision is to be a catalyst for a sustainable society. Within that sustainability framework is climate change. Also, our co-operative values compel us to address needs of Canadians that come as a result of

¹ Swiss Re, *Natural Catastrophes and Man-Made Disasters in 2013: Large Losses from Floods and Hail; Haiyan Hits the Philippines* (www.swissre.com/sigma/?year=2014#anchor0, 2014).

climate change. The question is no longer preventing the climate change, but adapting to climate change. So how can we better prepare our communities to deal with it?”

Background on The Co-operators

The Co-operators Group Ltd. is a Canadian-owned and -operated company with more than \$35 billion in assets under administration and two million people insured across the country. Originally formed as a co-operative by farmers to take care of themselves and their communities when traditional insurers would not meet their needs, The Co-operators has maintained this emphasis on community while expanding in size.

Climate Change Adaptation Strategy in an Insurance Firm

The Co-operators adopted a proactive approach to managing climate change risks and opportunities by creating an adaptation strategy. They were well positioned for two reasons. First, they could create insurance products directly related to damages caused by extreme weather events associated with climate change. Second, their business model as a co-operative enabled them to focus on addressing the unmet needs of their clients even when there were financial challenges to doing so.

The key question for The Co-operators senior management was how to provide adequate coverage for their clients at a price point that would be affordable while preserving the organization’s financial strength. This question became more pressing after the Alberta events, especially given Canada’s status as the only G7 country that does not provide overland homeowner’s flood insurance products.² A further challenge: although insurers did not provide flood insurance products, almost 70 per cent of Canadian homeowners believed their insurance policy fully covered them for flooding.³

The Co-operators has strong commitment to sustainability from the CEO and the Board’s Sustainability and Citizenship Committee. Formed in 2007, this committee includes four of the 22 directors and the chair of the Board of Directors. This commitment provides a strong basis for adaptation efforts.

2 Jason Thistlethwaite and Blair Feltmate, *Assessing the Viability of Overland Flood Insurance: The Canadian Residential Property Market* (Waterloo, ON: Faculty of Environment, University of Waterloo, 2013).

3 Dan Sandink, Paul Kovacs, Greg Oulahan and Glenn McGillivray, *Making Flood Insurable for Canadian Homeowners: A Discussion Paper* (Toronto: Institute for Catastrophic Loss Reduction & Swiss Reinsurance Company Ltd., 2010), p. 54.

Two main components of their adaptation strategy were: a) creating new insurance products for Canadians and b) engaging with stakeholders to create more resilient communities.

A major focus was the flood initiative, which included a new insurance product and stakeholder engagement. Although The Co-operators had a flood initiative underway for several years, in 2014 they increased their efforts to complete the initiative after seeing Canadians suffering from the effects of climate change.

Figure 1 shows the three major steps of the flood initiative.

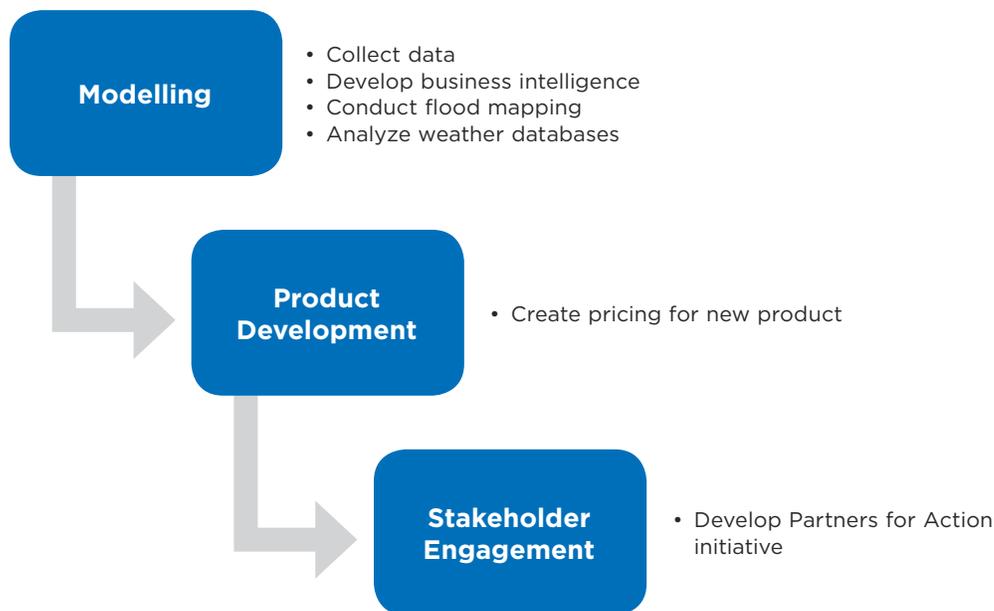


Figure 1: The Co-operators flood initiative

Below, we provide details on the initiative.

Modelling and Product Development

Home insurance has been traditionally referred to as fire insurance. But recently, more losses in homes have been due to water damage than to fire. The duration, intensity and frequency of weather events that threaten homes have increased, and floods have become one of highest risks associated with these events.⁴ Flooding affects properties and the well-being of residents: until the damage is repaired, they cannot return to their homes, send their kids to school nor resume their lives.

⁴ Jason Thistlethwaite and Blair Feltmate, *Assessing the Viability of Overland Flood Insurance: The Canadian Residential Property Market* (Waterloo, ON: Faculty of Environment, University of Waterloo, 2013).

The Co-operators thus saw an insurance product for floods as key to satisfying clients' unmet needs. "As part of our adaptation efforts, we attempt to respond with products, underwriting and claims practices that are relevant in today's environment and that provide our clients with clear and meaningful coverage options," said George Hardy, CPA, CA, vice president, Personal Lines and Underwriting. "Our desire to help our clients adapt to climate change is embedded in our corporate identity."

Hardy, a key participant in the development of this new product, described some of the major challenges:

- Developing a product solution that is simple, clear and comprehensive
- Identifying and quantifying risk
- Developing an approach to pricing
- Estimating Return on Equity (ROE) and Return on Investment (ROI)
- Creating awareness of the risk exposure related to water
- Making the business case for the new product

Stakeholder Engagement

The Co-operators thought of another way to help Canadians: by engaging with stakeholders to create more resilient communities. The Co-operators explored how they could leverage their relationships with other insurers, re-insurers, banks, developers, builders, government (federal, provincial and municipal) and non-governmental organizations (NGOs) to find a solution to the flood resiliency problem. As part of these efforts, they created Partners for Action, an initiative in collaboration with academics from the University of Waterloo. Partners for Action conducted research to find ways to reduce risks to the Canadian residential property market from overland flooding. The initiative involved diverse stakeholders, including property and casualty insurers, government policymakers, flood risk experts, professional associations, businesses and the legal community.

"There is a pre-competitive space where businesses can work together and find a solution, particularly around adaptation for cities. This is something that can be done," said Barbara Turley-McIntyre, senior director, Sustainability and Citizenship.

The Role of Accountants

The Co-operators relies on their accountants to help them make sound, financially disciplined decisions. While many parts of the business could see individual financial information pieces, finance teams were uniquely positioned to help the business understand the impact, down to the bottom line. Finance teams understand risk assessment, tax implications, capital planning, financial management and performance management: all critical concepts in business decision-making around climate change adaptation initiatives.

“Accountants really understand numeracy and numerical analysis. We also know we excel at big picture thinking; that is, seeing an issue from many angles and coming at it from diverse directions, as well as understanding business issues from the top line to the bottom line.”

George Hardy, CPA, CA, vice president, Personal Lines and Underwriting

Accountants were involved in other adaptation-related efforts apart from the flood initiative. For example, The Co-operators internal audit department verifies aspects of the annual sustainability report and reports to the senior management team and the Board audit committee on any issues with respect to how certain data were collected and verified.

Although accountants helped with the development of the new insurance product, some barriers prevented them from assisting to their full potential.

- **Resource constraints/work effort prioritization.** A primary barrier to accountants’ involvement relates to finance’s willingness and capacity to be involved and the business’s willingness to pay for it. “Finance teams follow a rhythm of monthly, quarterly and annual reporting as well as budgeting, which consumes their time,” explained Hardy. “The business does not follow the same pattern. To be involved, accountants have to be available when business needs them and it would need to be a priority. The business will also have to pay for the financial support.”
- **Focus on cost.** Accountants tend to be more focused on cost and less focused on value, George Hardy noted. Part of this emphasis comes from what the business has typically expected from accountants. Accountants could have added more value to the business case process if they had viewed it more as a tool to support achievement of business objectives and less as a costing and budgeting exercise.

The Future Role of Accountants

What competencies could companies such as The Co-operators benefit from in future work on adaptation? The Co-operators staff who were interviewed identify these areas for future contributions.

- **Providing context to quantitative analysis.** Accountants could carry out data analysis and link this analysis to the context of a real business problem, something that Turley-McIntyre called “head and heart coming together.” For example, in some countries, governments and companies have been trying to understand the ratio between dollars spent before and after extreme weather events. Accountants could help determine these calculations and assist with resource-allocation decisions.
- **Understanding Environmental, Social, Governance (ESG) issues.** Accountants could contribute more to adaptation if they had a deeper understanding of ESG issues, including climate change. “When I started my career 20 years ago, I had no idea I would be talking about climate change as a CFO and that it would be connected to what we are doing as part of our overall performance management of the organization,” said West.
- **Managing new data.** New informational resources are available. Hardy pointed to “the opportunity to take new data sets and all the new information that’s available to us now, along with the models that accountants are great at developing, and to use new capabilities with computing power...to take the quality of our decisions to another level.”
- **Valuing natural capital.** “Ten years ago, we did not realize that we should value our lakes, rivers and forests. The question is: how can an accountant bring that value of natural capital when planning a project that is, for example, manufacturing or mining?” said Turley-McIntyre. Accountants can support the adoption of natural capital accounting in their organizations and ensure that natural capital externalities are reflected in data collection, decision-making, cost benefit analysis, risk management and reporting.
- **Supporting and conducting stress testing and scenario analysis.** Stress testing and capital adequacy requirements have evolved; understanding of business risks has increased. Accountants, with their actuarial counterparts, have traditionally run those tests to ensure organizations maintain minimum capital requirements to reflect their underlying risks. “Accountants could help apply these concepts to climate change risks,” said Wesseling.

Case Summary

- *What is the business impact from climate change?*
Providing competitive coverage for the risks faced by clients from more frequent and intense weather events.
- *What is the adaptation strategy?*
Creating new products and motivating change that will create more resilient communities.
- *What is the current role of accountants?*
Accountants are part of the finance decision support teams, helping the organization make financially sound decisions.
- *What is the future role of accountants?*
Provide context to quantitative analysis, understand ESG issues, manage new data, value natural capital and support and conduct stress testing.

This case study was written by Sakis Kotsantonis, KKS Advisors, based on interviews with The Co-operators staff.



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