Climate Change Risks to the Insurance Sector

IAIS-A2ii Consultation Call, 15 November 2018
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CLIMATE RISKS AND INSURANCE SUPERVISION:
THE JOINT IAIS/SIF ISSUES PAPER ON CLIMATE CHANGE RISKS TO THE INSURANCE SECTOR

SUSTAINABLE INSURANCE FORUM

IAIS/A2ii CONSULTATION CALL

NOVEMBER 15TH, 2018
OVERVIEW

- **Climate risks are an emerging supervisory priority:** Understanding potential impacts on safety, soundness, stability of firms and markets

- **A rapidly evolving global agenda:** Climate risks central to policy action on sustainable finance in many countries, and at global level

- **Sustainable Insurance Forum:** International platform for supervisory collaboration on sustainability issues (focusing on climate change)

- **Issues Paper:** Raise awareness of climate risk issues, current and contemplated supervisory approaches, remaining knowledge gaps

- **2018 Activities:** Tools & training materials for climate risks, supporting TCFD Implementation, Capacity building

- **Recent Meeting:** November 10th 2018, Luxembourg
2013-2017: A doubling of policy and regulatory measures implemented by public authorities to align financial systems with sustainable development

**Insurance**: a starting point for central banks and supervisors seeking to examine how climate risks may have micro/macro prudential implications
ABOUT THE SUSTAINABLE INSURANCE FORUM

What is it?
• Global network of insurance supervisors and regulators working together to strengthen responses to sustainability challenges facing the insurance sector

What does it do?
• Platform for international collaboration among supervisors, facilitating knowledge sharing, dialogue, and uptake of policy innovations
• Convenes supervisors, makes consensus statements on sustainability optics, expert input on sustainability topics, produces research outputs

How does it work?
• Convened by UN Environment, bringing together the Inquiry and Principles for Sustainable Insurance (PSI) initiatives

Engagement with IAIS?
• Works collaboratively with IAIS Secretariat, meetings alongside IAIS events, produces research outputs with the IAIS
**Insulation 2030 Report:**
Suggests establishment of intl. forum for regulators on sustainability issues

**UK:** Bank of England PRA confirms support for a sustainable insurance forum as part of its climate review

**Budapest, June 2016:** SIF Planning Meeting alongside IAIS Global Seminar

**San Francisco:** SIF Inaugural Meeting, co-hosted by California Department of Insurance

**COP 21 Paris Climate Agreement:**
Finance flows consistent with low-C, climate-resilient development

**Financial Stability Board:** TCFD Recommendations for climate-related financial disclosures, with supplemental guidance for insurers

**Agenda 2030:** $90 trillion in financing; insurance critical across SDG framework

**UK:** Bank of England PRA confirms support for a sustainable insurance forum as part of its climate review

**October 2017:** Third SIF Meeting, Kuala Lumpur

**July 2017:** Second SIF Meeting, Windsor, UK
Argentina: Superintendencia de Seguros de la Nación (SSN)
Australia: Australian Prudential Regulation Authority (APRA)
Belgium: National Bank of Belgium (NBB)
Brazil: Superintendência de Seguros Privados (SUSEP)
Costa Rica: Superintendencia General de Seguros de Costa Rica (SUGESE)
France: Autorité de Contrôle Prudentiel et de Résolution (ACPR)
European Union: European Insurance and Occupational Pensions Authority (EIOPA)
Germany: Bundesanstalt für Finanzdienstleistungsaufsicht (BaFin)
Ghana: National Insurance Commission (NIC)
Guernsey: Guernsey Financial Services Commission
Italy: Istituto per la Vigilanza Sulle Assicurazioni (IVASS)
Japan: Financial Services Agency (FSA)
Morocco: Autorité de Contrôle des Assurances et de la Prévoyance Sociale (ACAPS)
Netherlands: De Nederlandsche Bank (DNB)
Singapore: Monetary Authority of Singapore (MAS)
South Africa: Financial Services Board (FSB)
Sweden: Finansinspektionen (FI)
United Kingdom: Bank of England Prudential Regulation Authority (PRA)
United States – California: California Department of Insurance (CDI)
ACTIVITIES TO DATE

• **Launch Meeting**: December 2016 (San Francisco, USA), co-hosted by California Department of Insurance
  
  • Established the Forum as an entity, agreeing framework document, governance, operations

• **Second Meeting**: July 2017 (Windsor, UK), Participants and observers from 17 jurisdictions
  
  • Joint statement in response to FSB TCFD, Knowledge sharing on climate risk

• **Third Meeting**: October 2017 (Kuala Lumpur, Malaysia)
  Two-day working meeting focused on content
  
  • Agreement to develop joint Issues Paper on climate risks from internal documents and survey materials

• **Fourth Meeting**: May 2018 (Rio de Janeiro, Brazil), alongside two other sustainability events
  
  • Finalizing Issues Paper and outreach strategy, review of Question Bank, proposals for new research
1. **Introduction**
2. **The Climate Risk Landscape**
3. **How Climate Change may Affect the Insurance Sector**
4. **Strategies for Insurer Climate Resilience**
5. **Relevance for Insurance Supervisors**
6. **Applicability of Insurance Core Principles for Climate Change**
7. **Supervisory Approaches to Climate Change Risks**
8. **Observed Practices: Case Studies**
9. **Conclusions**
Climate factors affecting insurance firms can be grouped down into two main categories of risks:

i. **Physical Risks**, arising from climate trends (i.e. changing weather patterns and sea level rise) and shocks (i.e. natural disasters and extreme weather events such as storms, drought, and heatwaves).

ii. **Transition Risks**, arising from disruptions and shifts associated with the transition to a low-carbon economy, motivated by policy, market, technological, or reputational factors affecting the value of financial assets.

Climate risks pose different strategic, operational, and reputational risks to insurance firms, across:

- **Underwriting Activities**, with wide ranging impacts across business lines (i.e. General, Life and health) and reinsurance
- **Investment Activities**, with impacts across financial instruments – including long-term debt securities (i.e. Sovereign debt, real estate)

While impacts may diverge between types of firms, over the long term, climate change is likely to hold major implications for the entire insurance sector – and all insurance firms.
## Relevance for Supervisors

### Core Objective

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<th>Core objective</th>
<th>Implications of Climate Change</th>
<th>Potential Responses</th>
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| Solvency and stability of insurance firms           | Potential for physical and transition risks to pose risks for solvency of individual firms, stemming from underwriting and investment activities | • Supervisory engagement to quantify potential financial risks associated with physical climate damages (i.e. underwriting liabilities)  
• Surveys and Disclosure requirements                |
| Market conduct, consumer protection, access and affordability, compliance | Potential for climate change render assets uninsurable (redlining); transparency for consumers on climate change practices and strategies; delivering enabling conditions for insurance product development | • Assessment of firm conduct on climate change issues  
• Supporting consumer awareness and literacy  
• Engagement with other policymaking bodies            |
| Macroprudential stability                            | Potential for transition risks issues to pose systemic risks to the financial system and macro-economy | • Assessments of exposure to high carbon assets risk  
• Alignment of investments with climate goals          |
ICPs set out a framework for supervisors to address the insurance sector with respect to climate change – as a new and emerging risk

First time an international financial authority has examined climate risks in relationship to core standards

Clarifies relevance of climate change risks across wide range of supervisory objectives and core functions, laying groundwork for global uptake

- ICP 7 (Corporate Governance)
- ICP 8 (Risk Management and Internal Controls)
- ICP 15 (Investment)
- ICP 16 (Enterprise Risk Management for Solvency Purposes)
- ICP 19 (Conduct of Business)
- ICP 20 (Public Disclosure)

Strong links to FSB TCFD Recommendations and Supplemental Guidance for Insurers – both as underwriters and asset owners
SUPERVISORY APPROACHES TO CLIMATE RISKS

1) Assessing Climate Change as an Emerging Risk
   • Mandates and Objectives
   • Initial Assessment
   • Signaling Expectations

2) Responding to Climate Change risks through Supervisory Practice
   • Risk Frameworks
   • Information and Data Gathering
   • Engagement Strategies and Examination Tools
   • Stress Testing for Physical Risks
   • Examining Transition Risks: Exposure Assessments, Scenario Analysis, Alignment Evaluation

3) Collaboration and Cooperation
   • Convening
   • Engaging with other public authorities
   • International Engagement
CASE STUDIES

- **Australia**: Australian Prudential Regulation Authority (APRA)
- **Brazil**: Superintendência de Seguros Privados (SUSEP)
- **France**: Autorité de Contrôle Prudentiel et de Résolution (ACPR)
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- **UK**: Bank of England Prudential Regulation Authority (PRA)
- **USA** – National Association of Insurance Commissioners (NAIC)*
- **USA – California**: California Department of Insurance (CDI)
- **USA – Washington State**: Office of the Insurance Commissioner (OIC)
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- **USA** – **Washington State**: Office of the Insurance Commissioner (OIC)
• Climate risks present significant material challenges for the insurance sector, which are likely to grow over time.

• Emerging consensus that the potential systemic impacts of climate risks require a global response (i.e. FSB, G20) – creating imperative for IAIS to act

• “It is imperative that resilience to climate risks be achieved by all insurers, regardless of size, specialty, domicile, or geographic reach.”

• “Climate risks will require ongoing and intensifying scrutiny by supervisors… (who) should seek to increase understanding of climate risk, and develop supervisory capabilities to be able to accurately evaluate the insurance sector’s actions to achieve climate resilience.”

• Additional supporting material from the IAIS and the SIF on best practices for addressing climate risk issues may be helpful for supervisors and insurers.
2018 Activities and Next Steps

Sustainable Insurance Forum
**NEXT STEPS**

- **Fifth SIF Meeting:** Saturday November 10\(^{th}\) 2018, immediately following IAIS annual conference (Luxembourg)

- **Supporting IAIS on Climate and Sustainability:** Engaging with IAIS its response to the TCFD, and other issues, as part of SPFO process.

- **Working with NGFS:** SIF accepted as an Observer institution in June 2018, planning to engage across work tracks where useful.

- **Broader engagement on sustainable finance:** Contributing, where appropriate, to national, regional, and global policy dialogue.

- **Exploring new Partnerships:** Working with other leading institutions to undertake research, capacity building and support implementation.
www.sustainableinsuranceforum.org

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Thank you.

Follow us on Twitter @a2ii_org, Youtube and LinkedIn

The Initiative is a partnership between: