



thinkpiece

Promoting debate and fresh thinking in the Insurance and Finance Industry

ClimateWise: the Insurance Industry Challenging Itself to do More

Andrew Voysey

Summary

- ClimateWise is a grouping of insurance firms and related organisations aiming to work individually and collectively to reduce the economy's and society's long-term risk from climate change. Its members represent 60% of the UK general insurance market and approaching 50% of the UK life insurance market.
- This article introduces ClimateWise and the role that this insurance industry initiative plays in challenging itself to do more to reduce the risks of climate change. The grouping has six core principles that provide a voluntary framework for action in agreed areas including leading in climate-related risk analysis and helping to inform public policy making at all levels.
- The article then explores the concept of 'systemic climate risk' and asks what it means to the insurance industry and what the industry's reaction to this challenge might be. Some insurance companies are calling for stronger government action to incentivise the transition to a low carbon economy, with their view of managing long-term risk uppermost in mind. This includes input into the Climate Change Bill and its legally binding emissions-reduction targets and associated carbon-budgets.
- However, there exists an important debate over the industry's role in promoting the move to a low-carbon economy. On one hand insurers might be expected to play their fullest role in driving such a transition by withdrawing cover from carbon-intensive industries; on the other it is not the role of insurers to play politics, and insurers exist to provide cover for the risks that society wishes to face.

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CII Introduction: in the midst of global recession it is tempting for stakeholders especially policymakers to diminish the importance of climate change. Indeed this is a challenge confronting many insurers, and the importance of staying the course cannot be overestimated. ClimateWise is an insurance industry grouping that counts the CII among its more recent members. In this second instalment of the CII's special series of thinkpieces on climate change, ClimateWise's secretary Andrew Voysey gives his personal view of the industry's developments and challenges at this crucial juncture.

One of the recommendations of the independent ClimateWise One Year Review, carried out by Forum for the Future – the UK Sustainable Development charity – argued that,

“The reliance of society on carbon-intensive industries creates climate risk, which will have a negative impact on all areas of the economy, including the insurance sector. Current business models within the insurance industry offer no incentives to link the evaluation of short-term risk with the long-term systemic risk arising from climate change. Insurance companies, in common with other parts of the economy, should take into account long-term climate risk in their business decisions.”

This clearly poses significant challenges to the insurance industry and is not an area where there are easy, or even well-understood, answers. But this takes nothing away from its significance. This ThinkPiece explores the concept of ‘systemic climate risk’ and asks what it means to the insurance industry and what the industry’s initial reaction to this challenge might be. First, it introduces ClimateWise and the role that this insurance industry initiative plays in challenging itself to do more to reduce the risks of climate change.

Challenge and co-operation

ClimateWise members are very clear that climate change is happening now and its impacts are being felt across our societies and economies. Insurance helps people to protect themselves against the risks associated with everyday life and plays an essential role in supporting, and underpinning, the economy and catalysing change.

The UK Government's legally binding commitment to reduce carbon dioxide emissions by 80% by 2050 is, essentially, a commitment to totally decarbonise our current way of life over the next few decades. A comparable global agreement

covering the developed economies is expected to be delivered in December 2009 at the next UN climate change negotiations in Copenhagen. It is anticipated that the developing economies will follow shortly afterwards.

In order to respond to the enormity of this challenge and to ensure that the response delivers new opportunities for long-term economic growth, individuals, businesses and countries will have to ask themselves big, hard questions and work together in new and innovative ways. It is this spirit of challenge and co-operation that led to ClimateWise's inception.

As ClimateWise's most recent member, the Chartered Insurance Institute is already playing a crucial role in stimulating and shaping the debate that is so necessary within the industry to understand why business-as-usual simply cannot go unchallenged in the face of irreversible climate change. As HRH The Prince of Wales, who launched the ClimateWise Principles in September 2007, says so often, time is a luxury we do not have. As such, the thought leadership sought by the CII is critical if this profession, so well versed in understanding and managing risk, is to respond to this challenge proportionately and appropriately.

What is ClimateWise?

At the heart of the initiative sit the six ClimateWise Principles, which were designed by the industry to reflect the core strengths and areas of influence of insurers. The Principles commit ClimateWise members to leading in climate-related risk analysis, using their knowledge to support climate awareness amongst customers as well as incorporating it into their own investment strategies, and helping to inform public policy making at all levels. Furthermore, the Principles commit members to reducing the environmental impact of their own organisations as well as reporting on an annual basis on actions taken so that they remain accountable at the highest level. These Principles are holistic and stretching – and rightly so – and we know that they are seen around the world as the global minimum standard.

We now have 40 members, including many international insurance brands and represents 60% of the UK general insurance market and approaching 50% of the UK life insurance market

Ultimately, ClimateWise members aim to work individually and collectively to reduce the economy's and society's long-term risk from climate change. We now have 40 members, including many international insurance brands, and represent 60% of the UK general insurance market and approaching 50% of the UK life insurance market. We continue to talk to

insurance organisations based all around the world and expect our membership to continue to grow.

Motives for action

What motivates insurers to commit themselves to the ClimateWise Principles? Naturally, there are a variety of interplaying drivers including changing customer demands, corporate reputation, brand differentiation and cost savings achieved through improved operational efficiency. But what makes the conversation so powerful, and sustains its momentum, is the relationship between a changing climate and the core business of insurers.

Indeed one leading asset manager now routinely asks insurance companies in which it invests whether they comply with the ClimateWise Principle as an indicator of good corporate governance and risk management

Questions about the reduction in insurability, the affordability of that insurance and even insurance market failure are influential, both for insurance leaders looking to what the future may bring and for investors looking to pick future winners. Indeed one leading asset manager now routinely asks insurance companies in which it invests whether they comply with the ClimateWise Principle as an indicator of good corporate governance and risk management. And of course, there are many new market opportunities, and indeed new markets themselves, that are already emerging as part of the solution to climate change and these are equally as powerful motivators.

So this is a mainstream strategic issue for this industry and that is a message that comes from its leading brands and bodies. Above all, ClimateWise members believe that the long-term stability of our economy depends on an appropriate response to climate change and it is to the benefit of all that they incorporate the risks from climate change and the need for mitigation into their business strategies. This is somewhat more fundamental than “going green for green’s sake”.

What do ClimateWise members do?

The ClimateWise Principles provide a voluntary framework for action – six agreed areas of priority that, if harnessed to their fullest extent, can leverage huge potential within the existing skill set, experience and influence of the industry. Being such a diverse industry – ranging from general to life products, primary to re-insurers, brokers to risk modellers, professional bodies to asset managers – these areas of priority will mean different things to different players. This

diversity of approach is welcomed. Flexibility in assessing compliance is crucial. But fundamentally, membership of ClimateWise is a commitment to action that is bringing a whole industry together to focus on one, global challenge.

With the facilitation of the ClimateWise Secretariat, run by the University of Cambridge Programme for Sustainability Leadership, members share good practice, come together for joint learning events, form special interest working groups and engage directly, and collectively, in the public policy arena to better articulate the expertise and role of the industry. The underlying philosophy of this voluntary engagement relates to learning, sharing, challenging and seeking greater impact through collective action. This makes ClimateWise unique in industry terms and the group strives towards a leadership position within their sector to ensure the momentum of change continues.

Achievements to date

So what has ClimateWise achieved to date since its launch in September 2007? What differentiates ClimateWise from other voluntary initiatives is the commitment by members to report publicly and annually on their actions against the ClimateWise Principles. After the first year, the entire membership honoured this commitment, which is a testament to the spirit of the initiative’s members.

The next stage was to seek an objective assessment of what had been achieved so far by ClimateWise members. Climate change presents us with new and difficult challenges, so it is important to use opportunities like this to reflect on how our journey is looking so far. So we appointed an independent organisation, the UK Sustainable Development charity, Forum for the Future, to carry out the first annual review. In particular, we tasked them with analysing the success stories to learn from, as well as areas for improvement in the future.

The headline finding was that, in its first year, ClimateWise has led to the insurance industry increasing its influence on issues of managing climate change as well as raising the awareness amongst the industry’s customers that this is a major problem.

The report acknowledged that the vast majority of members are taking the lead in risk analysis, through research into future risks posed by climate change, but members need to do more to incorporate climate change into their investment strategies - only half currently do so - and the report recommends actions to speed up the pace

of change which it sees as necessary to tackle the problems posed by climate change.

These include companies developing products and services in new areas related to climate change, including corporate liability and insurance for carbon markets and rainforests, as well as making their pension funds aware of the implications of climate change for company shareholder value creation.

The findings of this review provide a benchmark for members for their actions in the second year of membership. Meanwhile, efforts have also focused on the United Nations Framework Convention on Climate Change (UNFCCC) negotiations in Poland last December. ClimateWise members worked together to draw up a public statement on the talks to indicate what outcomes would enable the industry to play its fullest role in risk management and we were soon invited by the UNFCCC's Executive Secretary, Yvo de Boer, to deliver the statement to him in person during the negotiations.

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Many of the world's media were present as the ClimateWise group's statement calling principally for measures to strengthen climate change adaptation frameworks, was handed to the Mr de Boer. His response reflected the group's importance on the world stage. He said: “The insurance industry has a vital role to play. Its ability to offer insurance based on better risk management can guide governments to more effective policy decisions – both at the national and international level.”

Mr de Boer's words were most encouraging as was the acknowledgment at the UN that adaptation, alongside mitigation, is key to enable insurers to manage more effectively the risks brought to individuals and businesses across the world by climate change.

The year ahead

ClimateWise has two main objectives for 2009. First, we must achieve an increase in all members' delivery on the ClimateWise Principles to demonstrate year-on-year progress on this journey. Second, we aim to extend both the reach and influence of ClimateWise, primarily through a growing membership. Our participation at the UNFCCC shows that the importance of the insurance industry in coming up with workable

solutions to manage systemic climate risks is recognised at the highest level.

But is there an elephant in the room?

Which leads us back to the concept of systemic climate risk and the role of insurance. Quite apart from the international scientific consensus for action, the political rhetoric now talks of the transition to a low carbon economy being “inevitable”. In the UK, this case is made with direct reference to the Climate Change Bill and its legally binding emissions-reduction targets and associated carbon-budgets. Some insurance companies are calling for stronger government action to incentivise this transition, with their view of managing long-term risk uppermost in mind.

Carbon-intensive industries are still commercially viable at current carbon prices and will almost certainly form an important part of the economy for years to come. In the absence of regulation and with a carbon price that has plummeted following the worldwide slow-down in economic output, there is a view from outside of the industry that asks whether sectors such as insurance can do more now to drive the transition to a low carbon economy. Fundamentally, this thinking stems from the perception of the insurance industry as a leading communicator of risk – the messenger that indicates to individuals, businesses, society and governments how manageable the risks we face are, or are likely to be in the future.

Whether this perception itself is an important factor in the debate is worth dwelling on separately. But what role can ClimateWise play in the overall debate? As stated at the outset, this is not an area where there are easy, or even well-understood, answers. ClimateWise is certainly not professing to offer them, but here I explore the issues at stake in the debate; at the very least, to do so begins to respond to the external perception that the question remains an unaddressed ‘elephant in the room’.

Through informal exchanges with industry players, and certainly without representing formal or collective views, the problem seems to boil down to the challenge that insurers might be expected to withdraw cover from carbon-intensive industries in order to play their fullest role in driving the transition to a low carbon economy.

The instinctive response is that this would be to play politics, which is the role of governments not insurers. The argument is made that insurers exist to provide cover for the risks that society itself wishes to face and that if, through government, society wishes to alter the range of

those risks, then insurers will respond accordingly.

Similarly, when the issue of preferential rates pertaining to varying degrees of carbon-intensity of a given activity is considered, questions can arise around one company's vulnerability to competitors not acting in the same way or the implications of joint action in relation to competition law.

It could be argued that those insurers that are properly responding to the materiality of climate risk in their investment decision making are already sending strong signals to the market

An external perspective would argue that this is all a defensive excuse for inaction – a “passing of the buck” to government, which will itself never act strongly enough unless it feels a mandate for action from society and business. So is it that the industry has other roles to drive the low carbon transition and to create this political space?

There might be something of a more positive response here. For instance, it could be argued that those insurers that are properly responding to the materiality of climate risk in their investment decision-making are already sending strong signals to the market.

More broadly, the industry's role in facilitating and championing solutions to climate change is often cited as a powerful and realistic means by which insurers can drive the transition to a low carbon economy. Putting the political debates around the efficacy of carbon markets, mass roll-out of renewable energy, financial instruments to ensure the longevity of the rainforests or plans for carbon capture and storage aside, all require comprehensive insurance to have any chance of growth and success. Yet all contain certain degrees of new risks. These require the urgent and full attention of industry experts, in many

cases to ensure that legislation governing their rollout takes appropriate consideration of what the industry can and cannot accommodate in risk terms and in others simply to speed up the process.

Closing thoughts

This ThinkPiece has introduced the reader to what ClimateWise is all about, in theoretical and practical terms, and then exemplified one aspect of its role as the way the industry is pushing itself to do more by exploring the challenge of systemic climate risk. This is very much in line with the philosophies of learning and challenging that underpin the initiative. There are open questions about the roles of insurers and governments in society, whether the industry is playing its fullest role in driving the transition to a low carbon economy that it knows so well we need and what the next steps are. Thoughts and input from all sides would therefore be very welcome.

Above all, we must look to enhance the insurance industry's contribution to moving this planet onto a path where the risk of irreversible climate change is substantially diminished, thereby keeping the financial risks of our activities at insurable levels. Fundamentally, this is of core business interest to the industry and demands the attention and leadership of its greatest minds.

The thoughts and opinions expressed in this ThinkPiece are entirely those of the author and derived from the perspective that his position gives him. They do not reflect the views of ClimateWise or any of its members.

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