Position Paper

Insurance Europe comments on the IAIS draft Issues Paper on the implementation of the recommendations of the Task Force on Climate-related Financial Disclosures

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General comments

Insurance Europe welcomes the IAIS work on climate change and its endorsement of the Financial Stability Board's Task Force on Climate-related Financial Disclosures (TCFD) initiative.

The European insurance industry is fully aware of, and well-positioned to address, the financial risks posed by climate change and extreme weather, since the measurement of climate-related physical risks lies at the heart of insurers' business models. At the same time, insurers are continuously scrutinising their investment portfolios to incorporate long-term sustainability aspects and are increasingly considering the impact of transitioning to a low-carbon economy. Given the industry's concentration of expertise in managing, modelling and pricing climate risk, it is well placed to provide expert input where possible and so appreciates any opportunity to provide evidence and feedback.

In addition, European insurers support increased transparency around sustainable investments and sustainability risks, provided the provision of information is balanced and efficient. Therefore, insurers support disclosures that help consumers and investors to make informed financial decisions aligned with their objectives.

In particular, European insurers support the fact that:

- The IAIS is considering the implementation of TCFD recommendations in various **Insurance Core Principles (ICPs)**. Explicit references to sustainability in the ICPs will help strengthen the integration of material sustainability risks in insurers' operations in a consistent and efficient manner. In addition, this could be an effective way of ensuring minimum standards globally.
- The IAIS is taking a **coordinated approach between jurisdictions**, reflective of the cross-border nature of climate-related risks. Coherent policymaking between jurisdictions will avoid duplicative or contradictory standards.
- Supervisors encourage insurers to produce robust climate-related disclosures and consider **financially material climate-related risks** thoroughly, provided feasibility and proportionality considerations are taken into account. In this respect, the use of qualitative scenario analysis can be a useful way to measure climate risks.

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Insurance Europe also notes that:

- The implementation of TCFD recommendations through ICPs should allow sufficient flexibility for insurers to decide on the best way to deal with climate risks, in line with each company's specific characteristics and risk profile. Supervisors need to carefully assess the **appropriateness of TCFD recommendations** to the insurance sector and adapt them as needed if they should serve as a *de facto* standard.
- **Sustainability-related information** is a prerequisite for insurers to produce robust and efficient disclosures. Currently, quality data to accomplish the proposed disclosures is lacking, which has made it difficult for insurers to make as much progress as they would like on public disclosures and on communicating to relevant users. Regulatory support is needed to enhance the quantity and quality of ESG data available to insurers.
- Supervisors should investigate whether there are **disincentives** in the prudential frameworks, such as unjustified and excessive capital requirements, to support insurers' actions to mitigate climate risk. Insurers should not be undermined in their efforts by the regulations themselves.

Detailed comments on the content of the Issues Paper

Comments on section 1: Introduction

- **Paragraph 2**:
  - Given the magnitude and urgency of the issues at stake, collaboration between the industry and supervisors is fundamental to better understand and address climate-related risks. Therefore, it would be highly beneficial if the Sustainable Insurance Forum (SIF) would develop its collaboration and engagement with the industry, at least to reach the same stakeholder and industry engagement as the IAIS. Insurance Europe believes that the SIF should invite contributions, including stakeholder participation, from both industry and consumer groups.
- **Paragraph 3**:
  - The content and manner of the disclosures can develop naturally in markets eg via direct engagement with the users of this information, based on their needs. In view of this, it is vital that insurers are able to communicate climate impacts to their policyholders in a flexible manner to ensure information-users remain engaged, while recognising that consistency and comparability of information is also important. An overly prescriptive approach could lead to a lack of interest among users and their disengagement with disclosures. Disclosures to regulators, investors and other relevant market experts, however, could be far more detailed and technical than those to consumers.
- **Paragraph 6:**
  - The IAIS recognises that it is not clear "whether quality data to accomplish the proposed disclosures is available". This is a crucial point and creates a substantial challenge to fundamental policy positions within the paper.
  - The IAIS should better recognise the implications of limited data quality and availability of sustainability-related information throughout the Issues Paper. It is unclear whether the timeline for insurers' disclosure requirements will align with the timeline of disclosures from corporates and asset managers. The lack of quality data creates significant obstacles to the preparation of consistent public disclosures by insurers.
  - The IAIS should also make it clear throughout the paper that insurers should retain discretion over how they fulfil their responsibilities on climate-related public disclosures, while recognising the importance of consistency and comparability of information. Insurance Europe suggests replacing the last sentence with the following: "In addition, there has been no analysis of whether the recommended disclosures in the TCFD should be revised or enhanced to [better] address the issues of the insurance business or whether quality data to accomplish the proposed disclosure is available [without undermining the flexibility of disclosure.]"

Comments on section 2: Climate risk and insurance supervision: relevance of the TCFD Framework

- **Paragraph 20:**
  - Insurance Europe welcomes the IAIS plans to develop an Application Paper for supervisors on climate risks (covering ERM, investments, governance and disclosures) in 2020. It is crucial that policy divergence between jurisdictions is avoided where possible, to ensure a coordinated approach reflecting the cross-border nature of climate-related risks. This will avoid duplicative or contradictory standards between jurisdictions. Care should be taken to avoid overlaps between any new requirements and already existing requirements that ultimately satisfy the same objective.
- **Sub-section 2.3:**
  - Climate change is a global problem and so benchmarking good practices between supervisors internationally is clearly a necessity. Insurance Europe welcomes the fact that the IAIS sees various Insurance Core Principles (ICPs) as the mechanism by which TCFD recommendations could be implemented, since this could be an effective way of ensuring minimum standards globally.
  - Insurance Europe agrees that the wording of ICP 20 suggests that climate risks and TCFD recommendations are highly relevant to this principle and that climate-related information should therefore be within its scope. Insurance Europe also supports the incorporation of financial risks due to climate change into ICP 7 (corporate governance), including Board oversight and the broader management's role in assessing and managing climate-related risks and opportunities. In addition,

it supports the incorporation of financial risks from climate change into ICPs 8 (Risk Management and Internal Controls), 9 (Supervisory Review) and 16 (ERM and Solvency).
  - Explicit references to sustainability in the ICPs will help strengthen the integration of sustainability risks in a consistent and efficient manner to the benefit of policyholders. In particular, insurers should pay particular attention to financially material climate-related risks that have a high potential to affect the balance sheet of the insurance company.
  - In addition, supervisors' efforts to encourage insurers to make climate-risk disclosures in line with ICP 20 are supported, provided that TCFD recommendations remain voluntary and do not become an informal layer of duplicative disclosures on top of existing regulatory disclosures and tools already available in a given jurisdiction to deal with climate-related risks, eg with respect to the governance, actuarial and risk management functions. Therefore, Insurance Europe suggests adding a clear reference that implementation of TCFD recommendations through ICPs is aimed to encourage voluntary disclosures, rather than laying down the basis for future additional regulatory obligations.

Comments on section 3: Assessing TCFD implementation and climate-risk disclosure within the insurance industry

- Insurance Europe supports TCFD implementation. Further regulatory support is needed to enhance **the quantity and quality of ESG data available** in the wider financial system. It is important that implementation through the ICPs is not overly prescriptive and allows discretion to ensure that the presentation of information is suitable for its intended users, while recognising the importance of consistency and comparability of approaches. Implementation through the ICPs should support consistent and comparable climate disclosures across jurisdictions.
- Insurance Europe encourages the IAIS to consider how climate change will have an impact on the different types of insurance undertakings with **different timeframes for physical and transition risks**.
- Furthermore, as noted above, the IAIS should consider **the implications of limited data quality and availability** on sustainability considerations throughout the Issues Paper.
- **Paragraph 31:**
  - The result of the SIF survey should be disclosed to stakeholders, which in turn should have the opportunity to engage with the SIF. Indeed, this paper relies heavily on the SIF survey results, and on its implications, though none of these pieces of work have been disclosed. The IAIS should also consider other sustainability-related initiatives, similar to the TCFD, so that other perspectives not captured in the focused survey are reflected.
- **Sub-section 3.1.2:**
  - At present, there is an unfortunate and distinct lack of consistent market data on ESG criteria for insurers to use in their assessment of the financial risks associated with climate change. It is therefore important that TCFD recommendations are applied across the financial system including, for example, to fund managers. The IAIS should therefore work as collaboratively as possible, likely through FSB coordination, with supervisors and regulators of other financial market institutions.
- **Paragraph 37:**
  - Insurance Europe believes that supplementary guidance for insurance companies may need to be refined in order to better **reflect the specific characteristics of the insurance business** and to ensure disclosed information will not deliver wrong or misleading messages.
- **Paragraph 39:**
  - Insurance Europe notes that the paper compares insurers' awareness of climate change as a risk to insurers' actions to deal with it as proxied by the implementation of the TCFD recommendations. While Insurance Europe supports TCFD recommendations to promote information about climate-related risks and opportunities, it highlights that their implementation is not the only way for insurers to take actions to tackle climate change. In general, given the uncertainties in this area, European insurers make use of a number of good practices based on flexible, high-level principles that do not always fall under the TCFD recommendations, for example the United Nations Global Compact, the Carbon Disclosure report, ClimateWise Principles, UN Environment Programme - Finance Initiative, etc.

- In addition, Insurance Europe notes that the lack of materiality of climate risk will be the reason why undertakings do not explicitly disclose information about climate-change risks in their activities, including the nature of the insurance business (short duration of non-life contracts and ability to reprice them).

- **Paragraph 42:**
  - Insurance Europe recommends excluding the second sentence of the third bullet point of this paragraph on the applicability of the TCFD. Given the role of the application paper, the use of anecdotes should be avoided. The discussion should rather focus on evidence and take into account in a transparent manner the limitations of the SIF/IAIS survey, eg regarding country participation.
  - In addition, it should be noted that European insurers are aware of the TCFD recommendations and a number of them have in fact started to implement TCFD-aligned disclosures.
- **Paragraph 44:**
  - Insurance Europe notes that quantifying how climate-related risks affect business resilience is a difficult task for insurers. That said, risk modelling and risk management are a core expertise of the insurance industry and insurers have played a key and leading role in the development of models, leveraging on long-standing collaboration with the scientific community. In addition, insurers pay close attention to a number of factors that might be directly affected by climate change, eg mortality and morbidity assumptions.
  - Care should be taken to highlight the lack of climate-related data that insurers can use to improve their models. Therefore, public action to encourage the disclosure of quality (granular, consistent, etc.) climate-related observed data, including on climate-driven events, is supported. Similarly, the increased availability of data on sustainability considerations by companies across all sectors would facilitate insurers' risk assessments.
  - An appropriate balance should be struck between working with third-party service providers and developing insurers' own models, which can be used over a number of years. If not, the use of the complex methodologies of third-party service providers can make insurers excessively dependent on those third parties for year-on-year comparisons, which could create a black box for insurers and damage their ability to assess risks in the long-run.

Comments on section 4: The role of supervisors

- Insurers are fully aware of their responsibility for the sustainable development of society and the economy and are willing to take voluntary steps towards disclosure. Hence, supervisors should opt for a flexible approach (eg, guiding principles) rather than a prescriptive approach. This would allow insurers to embed sustainability considerations more easily in their business operations in line with their company-specific characteristics. To this end, it is important that supervisors:
  a) provide insurers with discretion on how they fulfil their responsibilities on climate-related public disclosures, while recognising the importance of consistency and comparability of information.
     While recognising the importance of consistency and comparability of disclosure approaches, the implementation of voluntary disclosures is an entity-specific decision which depends on whether the TCFD recommendations can be usefully and meaningfully applied to the specific business activity under consideration. In addition, policyholders and investors who are particularly sensitive to sustainability risks will actively ask for information about them.
  b) focus on the consideration of financially material climate risks.
     Small entities might be less exposed to some specific climate risks. Insurance Europe therefore considers it particularly relevant to primarily focus on dealing with financially material risks. Both the supervisory authority and the insurance entities should also ensure that the actual risk profile is proportional to the effort required to consider climate risks.
  c) clarify that the disclosures should take into account feasibility and proportionality considerations.
     It should be made clear that beyond materiality, disclosures should take into account feasibility and proportionality considerations. In particular, the IAIS work should not end up being a de facto informal disclosure obligation.
- **Paragraph 46:**
  - Insurance Europe welcomes the clarification here that the work on TCFD implementation aims to develop guidance, not legal obligations.

- **Sub-section 4.1:**
  - It will also be important going forward for the IAIS to consider how the Insurance Capital Standard (ICS) will be designed/implemented to ensure that climate risks are adequately reflected in the final regime.
  - The development of the ICS should incorporate a long-term perspective and consider opportunities as well as risks, as expressly acknowledged in the TCFD recommendations. It will be essential, for example, that **ICS capital charges** for sustainable infrastructure projects and other ESG investments do not disincentivise insurers from investing in these assets while continuing to be risk-based.
  - Given the long-term, illiquid nature of life insurers' liabilities, many are well placed to invest in long-term assets that contribute to the transition to a low- or zero-carbon economy. The IAIS should investigate whether the ICS calibration and design do not disincentivise sustainable investment so that the ICS does not undermine insurers' sustainability efforts. In addition, it should be clarified that the ICS calibration and design should remain risk-based. Finally, it is also worth emphasising that European insurers' use of internal models plays an essential role in adequately calculating risk exposures in areas such as catastrophe risks, which are a key element of climate risk.
- **Sub-section 4.1.1**:
  - The European insurance sector believes that climate-change risks should be considered as long as they are expected to have a material impact on an insurer's balance sheet. Despite the TCFD being a useful tool to enhance transparency, supervisors should first evaluate the applicability of TCFD recommendations and consider how they are tailored to the insurance sector in general and to companies' specific characteristics in particular. To achieve effective oversight, a balanced and flexible approach is needed and not a "one size fits all" approach.
- **Paragraph 50**:
  - Insurance Europe suggests adopting a principle-based approach that allows insurers sufficient flexibility to avoid potentially negative consequences and information duplication before moving to detailed reporting guidelines. Indeed, it is important to first assess the relevance and availability of the detailed information that would be required in a detailed reporting based on the specific characteristics of each insurer's business and risk profile.
- **Paragraph 51**:
  - Insurance Europe agrees with the IAIS that potential conflicts with other disclosures should be considered. The timing of disclosures remains a key issue of debate. Disclosing climate risk-related information and broader financial information at the same time might be challenging for insurers and place unnecessary pressure on them. Given the high complexity of the data to be processed, insurers should be given sufficient time to efficiently complete the required analysis. Timelines for disclosures should be defined according to the nature of the information and data. Timelines can be chosen so that they do not coincide with those of financial reporting.
- **Paragraph 52**:
  - Insurance Europe does not consider it useful to expect each legal entity of a group to deliver TCFD-aligned disclosure if the group is able to disclose on a group-wide basis supported by its established group governance on climate. Such a demand would place an unnecessary burden on insurance groups and create further complexity.
- **Sub-section 4.1.6**:
  - In relation to the Insights paper on climate risk assessment tools of the Financial Stability Institute (FSI) and SIF, Insurance Europe supports the use of **stress-testing and scenario analysis** as a useful way to facilitate informed discussion aimed at measuring climate risks, provided undertakings have sufficient flexibility. Insurance Europe would, however, recommend that, at least to begin with, IAIS supervisors place the onus on qualitative rather than quantitative scenario analysis, as this would lead to more robust testing. As the insight paper states, the numerical results are affected by high uncertainty, also as a consequence of limited data quality and availability.
  - In addition, standardisation should be carefully evaluated to avoid it becoming an impediment to the insurer carrying out a company-specific risk assessment.

- **Paragraph 54**:
  - Insurance Europe believes that it is too soon to state that the results of scenario analyses could influence product pricing and availability. It is essential that the scenarios and the associated impacts are developed and assessed based on robust scientific evidence. And then the results need to be analysed very carefully through active engagement with stakeholders before drawing any conclusion on the impact of the tests.
- **Paragraph 57**:
  - Insurance Europe believes that a progressive and phased approach is very important if supervisors want to make climate-risk reporting mandatory. It should be noted that not all TCFD recommendations automatically fit all insurance companies and that it will indeed be crucial to carefully assess the appropriateness and relevance of the TCFD recommendations' specific insurance guidance based on the specific characteristics of each insurer's business and risk profile. TCFD recommendations must be further adapted to the insurance sector if they are to serve as a *de facto* standard.
- **Paragraph 61**:
  - Insurance Europe believes that a wide disparity between insurers does not justify an additional layer of legally binding requirements. A voluntary and flexible approach will ensure the agility to reflect fast-changing developments in climate-related issues.
- **Paragraph 63**:
  - Insurance Europe recommends that the first bullet refers to national/local governments as well as consumers in relation to leveraging insurance sector intelligence in raising awareness, mitigation and adaptation.
  - Insurance Europe believes that the forward-looking scenario analysis referred to in the second bullet may be a useful tool to improve mitigation strategies and push for prevention actions. However, long-term scenarios should not be used at this stage to draw conclusions on capital requirements.