European Insurance and Occupational Pensions Authority

Workshop on Sustainable Finance

Summary of the workshop on sustainable finance organised by the European Insurance and Occupational Pensions Authority (EIOPA) on 11 June 2019 at EIOPA's premises in Frankfurt am Main

On 11 June, EIOPA organised its third discussion with stakeholders on sustainable finance. Those participating, on site and via videoconferencing, included members of EIOPA's Stakeholder Groups, the European Commission, consumer representatives, representatives of the insurance and pensions industries, of asset management and rating industries, and representatives of civil society.

In his welcoming remarks, EIOPA's Executive Director Fausto Parente stated that the topic of sustainable finance is a strategic area of work for EIOPA. He also stressed the need for insurers and pension funds to take into account the impact of their activities on the sustainability of the economy and environment.

He referred to the areas of work EIOPA has been engaging in during the recent months. In April, EIOPA delivered its advice to the European Commission on the integration of sustainability in the Solvency II Directive and the Insurance Distribution Directive. EIOPA is cooperating with stakeholders on a scenario analysis of climate-change related risks, and has started, together with the European Securities and Markets Authority (ESMA) and the European Banking Authority (EBA), to develop technical standards for the disclosure of sustainability risks and sustainable investments. Supervisory opinions with regard to Environmental, Social and Governance (ESG) risks and on Governance for Institutions for Occupational Retirement Provision (IORPs) are expected to be published this summer and supervisory activity will include the sustainability provisions within the IORP II Directive. At international level, EIOPA is actively engaging with the Sustainable Insurance Forum and the Network for Greening the Financial System.

He mentioned the upcoming report from the European Commission's Technical Expert Group on the proposed activities that contribute to climate change mitigation and adaptation. EIOPA supports the role which the (re)insurance industry can play in supporting climate change adaptation, or sustainable development more generally. In particular, more sustainable underwriting practices should contribute to achieving these goals. This is one of the areas addressed in the draft Opinion on integrating sustainability within Solvency II, which is under consultation until 26 July 2019.

Looking ahead, EIOPA will be collecting evidence on the short-term pressure on/from (re)insurers and IORPs and the potential implications for sustainability goals and undesired consequences for financial stability. EIOPA is being asked by the European Commission to deliver its report by end December 2019. He invited the participating stakeholders to provide their views and input to this collection of evidence.

EIOPA has also taken up the discussion on the (insurance) protection gap for natural catastrophe risks. The increasing frequency and severity of natural catastrophes, under the influence of climate change, can have systemic repercussions. This requires concerted European action in gathering relevant information and data and fostering innovation in modelling and risk transfer solutions.

He thanked the participants for their participation to the workshop and their upcoming contributions to the consultations and discussions.

Session 1: Consultation on the draft Opinion on sustainability within Solvency II

EIOPA presented the key elements of the draft opinion, which is under consultation until 26 July 2019 (Consultation on an opinion on sustainability within Solvency II). The following main points were addressed during the discussion:

- Capital requirements should not be used to promote certain (green) investments. Stakeholders would not support a specific calibration for sustainable assets. EIOPA has pointed out in its opinion that there is not sufficient evidence on a difference in risk profile for green investments, compared to general investments today.
- Scenario analysis by (re)insurers is considered a good way forward for embedding a more quantitative risk assessment of the effects of climate change. Standard requirements for scenarios, in particular for the ORSA, should help undertakings in establishing their practices in a proportionate manner. This may help small and medium insurers to assess risks on their assets and liabilities using available consistent scenarios. Challenges lie in the definition of the time horizon and the choice of assumptions. The exercise should not be confused with a public stress testing exercise or understood as to imply the public disclosure of the Own Risk and Solvency Assessment (ORSA) results.
- Further thought should be given to the integration of ESG considerations in the valuation of the best estimate for life and health insurance business. In addition, environmental issues beyond climate change would have to be considered going further (e.g. biodiversity or other sustainable development goals).
- There is support for integrating measures of climate risk adaptation in the underwriting policies, which should eventually contribute to lowering the risks to the underwriter.
- Investment practices with regard to climate change require a nuanced approach, which amounts to assessing the risk each investment poses to the climate.

Session 2: Call for advice on undue pressure for short-termism.

In February, the European Commission launched a call for advice for the three European Supervisory Authorities (ESAs) to collect evidence on potential undue pressure for short-termism from financial markets on corporations. The aim is to foster transparency and long-termism in financial and economic activities by exploring possible drivers of short-term pressures. During the workshop, EIOPA presented the approaches, the sources and the key steps foreseen to collect evidence. Building on available literature, EIOPA is analysing the portfolios' evolution over time and the asset holding periods' development. Among others, EIOPA is assessing the relevance of reporting frequency, remuneration policies and R&D trends on the investment decisions. EIOPA plans to make use of relevant work published on the insurance and occupational pensions sectors, as well as information already available from regular reporting or other existing information requests. EIOPA stands ready to engage with insurance undertakings on qualitative information to complement the quantitative information available at EIOPA, and beyond supervised entities. EIOPA invites the participants in the workshop to submit their views on particular questions or more broadly on the topic via the feedback statement on anonymous basis or bilaterally by email to the EIOPA Studies & Statistics team (St-team@eiopa.europa.eu).

The following remarks were made during the discussion:

- Shareholder expectations and remuneration schemes are potential drivers of short-term pressure on corporates. Pressure from activist investors for buy-back programs and dividend payouts from reserves, increase short-term pressure.
- On the other hand, stakeholders highlighted that insurance undertaking are mainly long-term investors, with their investment strategy being driven by their liability profile. Therefore, they should be less subject to short-term market pressures.
- Financial institutions are not always originators of short term behaviour but sometimes import the consequences of short term behaviours from external sources and transfer those to the investees (such as those arising from tax incentives, corporate reporting requirements).

Session 3: Protection gap for natural catastrophe risks.

EIOPA is keen to engage with stakeholders on a discussion concerning the widening of the (insurance) protection gap for natural catastrophe (NatCat) risks.

In light of climate change, the risk of an increasing frequency and severity of natural catastrophes is becoming more and more apparent. The insurance penetration varies across Europe and the impact of natural catastrophes across regions may change under the influence of climate change.

EIOPA is concerned that the impact of a protection gap on households and businesses as well as on the financial system will be systemic (losses affecting banking books, e.g. loss of collateral) and aggravated by public financing options of Member States.

Therefore, the potential widening of the protection gap for natural catastrophes in Europe requires a concerted European action.

EIOPA sought views of stakeholders on the role of the insurance industry, as well as of the public sector. Questions include how measures can contribute to achieving an optimal insurance penetration across Member States, securing affordability of insurance, and promoting adaptation, preparation as well as risk management incentives in (re)insurers' underwriting policies and product design. EIOPA stressed the need for commonly available data and analysis on NatCat events in Europe to raise awareness on risk management gaps and to anticipate solutions.

Following observations were made during the discussion:

- Stakeholders stressed the need for public solutions, considering that the primary issue would be affordability of insurance. Climate change is likely to affect the most vulnerable members of society, who may not be able to afford insurance.
- Education to citizens about risks and risk mitigating behaviour should be promoted to sustain insurability. Insurance policy conditions are likely to change in light of climate change and it is worth exploring this impact on the protection gap.
- Risk mitigation and adaptation should be the first safeguards against the widening of an (insurance) protection gap. The European Flood Directive was cited in this respect.