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SUSTAINABLE FINANCE

Green shoots

Insurers welcome the European Commission's renewed actions on financing sustainable growth

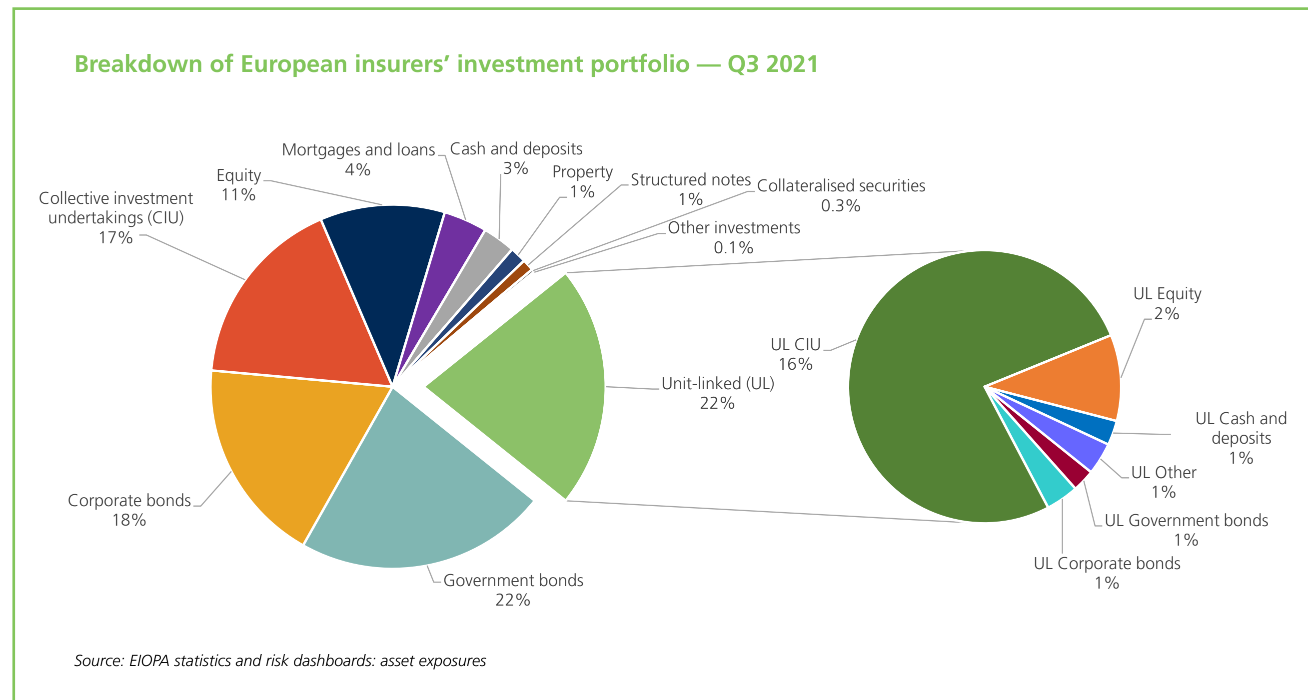
Climate change and environmental degradation are defining global challenges of our time. The European Commission estimates that €350bn in additional investment per year over this decade is needed to meet its 2030 emissions-reduction target in energy systems alone, in addition to the annual €130bn it will need for other environmental goals.

It is important that environmental regulation is complemented by a sustainable finance framework and the right regulatory changes to create the conditions that will allow public and private finance to be channelled to investment that reduces exposure to climate and environmental risks. Insurers recognise the need for urgent action, which has never been more unambiguous and, as demonstrated by the February 2022 IPCC report[1], the costs of abatement, mitigation and adaptation measures pale in comparison to the long-term costs of unmitigated climate change.

Potentially huge role for insurers

The European insurance industry supports the goals of the Paris Agreement and the European Green Deal, as well as the EU's ambitious targets to reduce its greenhouse gas emissions by 55% by 2030 and achieve a net-zero economy by 2050. Insurers can play a significant role both in mitigating the

1 "Climate Change 2022: Impacts, Adaptation and Vulnerability", IPCC, February 2022



Source: EIOPA statistics and risk dashboards: asset exposures

worst climate-change scenarios and in helping citizens and businesses to cope with and adapt to the impacts of the changes that cannot be avoided.

As Europe's largest institutional investor, with over €10.6trn of assets under management, the insurance industry is in a unique position to facilitate the transition to a more sustainable economy.

For many years, the industry has highlighted that three key areas of regulatory change are needed to allow insurers to play their full role in sustainable finance. Insurance Europe welcomes the fact that the Commission has launched initiatives covering each of these three areas.

The first is to improve the EU's Solvency II regulatory framework for insurers to remove the measurement flaws that unnecessarily constrain the industry's ability and willingness to invest long-term, including in sustainable investments.

The review of Solvency II, which is currently under discussion by the Council of the EU and the European Parliament, is the perfect opportunity to make these improvements. Insurance Europe welcomes the fact that the EC said when making its proposals that the "aim of [the] review is to strengthen European insurers' contribution to the financing of the recovery, progressing on the Capital Markets Union and the channelling of funds towards the European Green Deal". (See page 22 for more on the Solvency II review.)

The second area is the need for sustainability data to allow insurers, along with other investors, to identify sustainable investments and transition projects to finance. The EC has launched a very comprehensive set of sustainability reporting initiatives which, within a few years, are intended to generate the data that is needed. (See page 12 for more on sustainability reporting.)

The third area is the need for a significant increase in the supply of suitable sustainable projects and assets in which to invest. The potential capacity to invest is currently not matched by available assets. For example, in October 2021, the EC issued the first NextGenerationEU green bond to be used exclusively for green and sustainable investments across the EU. It was more than 11 times oversubscribed.

Insurance Europe welcomes the Commission's ambitious set of initiatives designed to encourage and require the wider industry to make the changes needed to achieve net zero by 2050 and fully take into account sustainability in how they operate. These initiatives are covered by the Green Deal and include the Sustainable Finance Strategy.

EU's renewed strategy is welcome

In 2018, the Commission adopted its first action plan on financing sustainable growth and followed it in July 2021 with its Renewed Sustainable Finance Strategy, which contains further welcome steps towards advancing the objectives of the European Green Deal and improving the funding of sustainable projects.

For insurers, the EC's proposal for an EU Green Bond Standard (EUGBS), currently going through co-legislator scrutiny in Council and Parliament, is a particularly important part of the renewed strategy.

Specifically, Insurance Europe welcomes the fact that, as proposed by the EC, the EUGBS:

- will help enhance the availability of attractive sustainable assets;
- will allow investment with confidence in EU green bonds, on the basis of reliable, comparable and standardised information;
- will facilitate sovereign issuance of green bonds;
- will be based on market standards, making it a potential future global standard for green bonds;
- will be voluntary and therefore will not prevent the use of other sustainability bond standards, thus avoiding potential negative effects on the fast-growing and international green bond market.

There are however some improvements that can be made to the EUGBS:

- **Grandfathering** — Under the current proposal, the EUGB designation is not maintained for the entire term of the bond up to maturity, which may result in lower attractiveness for investors and issuers. The regulation should therefore make it clear that outstanding EU green bonds, regardless of subsequent changes to the screening criteria of the EU taxonomy, remain EU green bonds.
- **Use of proceeds for transition** — For EU green bonds to support more new green projects and help achieve the objectives of the European Green Deal, it is vital that European green bonds allow the financing of transitional projects. For this to happen, the EU taxonomy for sustainable activities must be developed to fully embed transitional measures.
- **Accreditation** — Monopolistic market structures increase issuance costs and could act as barriers to issuing green bonds. The accreditation criteria and supervision for EUGB reviewers should therefore not result in situations in which ESG agencies hold market- and price-setting powers, such as in the credit rating agency market.
- **Flexibility** — The industry welcomes the added flexibility of a "flexibility pocket", which allows a small portion of expenditure from EUGBS proceeds not to be aligned with the EU taxonomy, given that companies make a reference to their transition plans as required by the Corporate Sustainability Reporting Directive and that general "do no significant harm" criteria are applied to scan proceeds that are not aligned with the taxonomy.
- **Taxonomy alignment** — The EU taxonomy for sustainable activities is based on criteria at activity level, while bond financing is usually at project level. Issuers will need some discretion over how to align projects under an EUGBS with the activity-based screening criteria (ie, how to apply the taxonomy at project level).

These improvements would ensure the uptake of the EUGBS.

Insurance Europe's Sustainability Hub

Europe's (re)insurers are contributing in a wide variety of innovative ways to combatting climate change and its effects and meeting sustainability goals.

The Sustainability Hub on Insurance Europe's website showcases the many ways that (re)insurers are compensating for losses, risk-modelling, raising awareness, developing new products and building sustainable investment portfolios.

The Hub also includes details of national public-private partnerships and of industry commitments, alliances and coalitions.