

Response to the EIOPA discussion paper on non-life underwriting and pricing in light of climate change

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Non-life underwriting and pricing

(para 2.1 to 2.38)

Q1: Do you agree that climate change could lead to increasing premiums and wider exclusions, potentially negatively impacting the affordability and availability of insurance covers over the long term?

<input type="checkbox"/>	Yes
<input type="checkbox"/>	No

Firstly, the wording of the question is misleading, as it seems to imply that there are no measures beyond pricing and deductibles to sustain the availability of insurance, when prevention, notably, plays such a crucial role.

Having said this, without the necessary action on both mitigation and adaptation, and from a purely financial perspective, climate change is indeed expected to negatively impact the affordability and availability of insurance for certain risks over the long term. However, focusing exclusively on pricing and deductibles does not reflect the way insurance business functions and it ignores the crucial role played by public authorities in adopting the necessary legislation for mitigation and prevention/adaptation.

Q2: Do current underwriting and pricing practices already take into account the expected impact of climate change?

<input checked="" type="checkbox"/>	Yes
<input type="checkbox"/>	No

The impact of climate change is often not fully clear, and in some instances data trends might not even matter, as singular weather events cannot be linked to specific trends. The analysis of historical data therefore plays a large role in the underwriting and pricing process, and through this the impact of climate change is factored into insurers' business *a posteriori*.

However, insurers take a holistic view of risk management across their processes and core business, and the monitoring of past climate-change-related events and losses is just one of the instruments used in the underwriting and pricing process.

Despite a number of data and methodological constraints (and the challenges in quantifying and analysing the long-term effect of climate change on pricing and resilience in business models), forward-looking analysis is also increasingly used in combination with historical assessments based on up-to-date data. This is focused on expected changes in the frequency and severity of certain events that are relevant for pricing yearly guarantees and the periodic adjustment of their conditions.

One important element of underwriting and pricing involves imposing certain conditions on contracts, such as prevention measures. These conditions are not necessarily based on past events but can also be the result of trend forecasting, increasingly over the longer term. This is clearly an example of the future/expected impact of climate change being incorporated in the underwriting/pricing process.

Finally, insurers' investment strategies have an effect on the underwriting/pricing process, and these investment decisions most definitely take into account sustainability risks and the expected impact of climate change in general, also by means of significant sustainable investment and energy transition commitments.

Q3: What are in your opinion the main obstacles to maintaining insurability and affordability in the context of climate change?

The lack of adequate action on mitigation and adaptation is the main obstacle to maintaining insurability and affordability in the context of climate change.

Focusing on natural catastrophes, it is essential for policymakers not only to take measures to mitigate the effects of climate change, but also to focus on adapting to its consequences. This means shifting the focus from reacting to (climate-change-related) natural catastrophes to a more proactive approach that prioritises prevention, risk reduction and resilience building. This, in turn, will help to maintain the insurability and affordability of these natural catastrophe as they become more frequent and severe because of climate change. While it is primarily the responsibility of public authorities to take action in this area, the insurance sector has the ability and willingness to contribute to the process of adaptation.

Without the necessary adaptation measures promoted by public authorities, insurers can only act within the confines of the basic insurance principles and regulatory framework, including solvency rules designed themselves to protect those same consumers seeking protection from natural catastrophes.

Collaboration between public authorities and companies can happen in many areas, such as, for instance, data enhancement and data exchange, which can facilitate the assessment of vulnerability to climate change, eg, the resilience of real estates.

In this respect, it is also noted that EIOPA proposes to improve differentiation and therefore limit solidarity between high-risk groups. Such a practice could lead to unaffordable premiums for certain risk groups, as each risk groups ends up paying for its own risk.

Options to ensure availability and affordability of insurance in light of climate change

(para 3.1 and 3.2)

Q4: Do you see a role for coordinated industry solutions or Public-Private Partnerships to maintain availability and affordability of insurance covers?

X	Yes
	No

Coordinated industry solutions and PPPs can and do play a role in maintaining the availability and affordability of insurance in the context of climate change. Insurers participate in PPPs to build community resilience, which in turn helps maintain insurance affordability and availability. Member states can also actively promote insurance in order to ensure adequate protection for their citizens. The nature of these solutions/partnerships and their roles vary according to the areas/risks to which they relate. As no such “one size fits all” solution is applicable at European level, these solutions should be defined at national level. In any event, they will never be sufficient, and it is ultimately for governments to take the decisive actions needed to enhance adaptation and address the protection gap.

Floods are a good example of this. National and local authorities should enhance resilience by implementing effective prevention measures: requests to build on flood plains should be denied (land-use planning), while flood defences for vulnerable areas should be maintained and reinforced, and building codes adapted (eg, building elevation). Flood Re in the UK has been set up to help to close the protection gap and reduce the impacts of future volatility from changes in climate risk [\[link\]](#).

Public authorities also have a key role to play in tackling the underinsurance of natural catastrophe risks in countries in which the protection gap is significant, and this can indeed be done through PPPs in certain areas or simply the active promotion of insurance for natural perils in others.

Q5: Do you think that insurers developing impact underwriting would impact positively or negatively the availability and affordability of insurance?

	Yes
	No

The definition of impact underwriting remains too vague to be able to state the extent to which it could impact the availability and affordability of insurance in the context of climate change, whereas the positive impact of prevention and adaptation in this respect is proven.

As evidenced by responses to the other questions, insurers already practise impact underwriting to an extent: they not only transfer and pool climate-change-related risk, but also contribute to reducing exposures to climate risks. This is clear with climate-change mitigation and adaptation where this is achieved through the features of their products or their investment strategies.

However, the assessment and pricing of any risk that the insurer is requested to cover must be exclusively risk-based at all times. Any change to underwriting/pricing practices must take place within the given regulatory framework, Solvency II in particular. Should this not be the case, the balance between risk-based premium income and claims payments as a foundation for financial market stability would be severely jeopardised. Other, non-risk-based aspects of sustainability should therefore be taken into account before or after the underwriting process.

In any event, developing impact underwriting would certainly not impact the availability and affordability of insurance in a way that would free public authorities from the need to take adaptation (and mitigation) actions.

Q6: Are you aware of other measures such as tax rules or local GAAP which could improve the availability of insurance cover for climate risks?

(In particular, some authors have suggested that governments could incentivise the building up of equalisation provisions to improve the availability of insurance cover for climate risks.)

X	Yes
	No

In the Netherlands, agricultural insurance cover for weather-related perils (*lato sensu*) is exempt from insurance tax as well as subsidised by the government.

Contribute to climate change adaptation or mitigation via risk-based pricing and contractual terms

(para 3.3 to 3.16)

Q7: Should underwriting and pricing practices make allowance for wider climate change considerations that go beyond direct impacts on the insured risk? Please provide examples in your answer and indicate what are the challenges to including such considerations, in particular how to comply with risk-based actuarial principles.

(Direct and indirect impact of insurer's contribution to climate change adaptation or mitigation on the insured risk: (a) direct - insurers contribute to climate change adaptation and mitigation and the insured risk is directly decreased (for example incentivise policyholder to take prevention measures against flood risk contributes to climate change adaptation and also directly reduces the insured risk) (b) indirect - insurers contribute to climate change adaptation and mitigation but it does not directly decrease the insured risk; it is expected to have an impact at long-medium term on the overall climate related risks exposure of the insurer (for example offering insurance coverage for photovoltaic panels does contribute to climate change mitigation but the insured risk is not directly impacted. The impact on the insured risk could be materialised in the future as GHG emissions are reduced on a longer term.)

X	Yes
	No

Insurers' underwriting and pricing practices already make allowances for wider climate-change considerations that go beyond direct impacts on the insured risk, as evidenced by the examples provided in the questionnaire. That being said, actuarial risk-based principles remain key and there must therefore still be a link between the reason for the discount and the risk insured.

The photovoltaic panels example is only relevant for natural catastrophe cover (which is made worse by climate change) and does not necessarily work for other types of cover (eg, fire insurance cover for buildings). The calculations will also be complicated by the fact that insurance covers are often bundled.

Furthermore, there is no systematic decrease in risk as a result of more sustainable behaviours, and a careful risk analysis is therefore still necessary. A discount on motor insurance for driving an electric car should only be provided if there is evidence that the insured risk is lowered one way or the other, even if just indirectly.

Q8: What role do you see for direct risk prevention measures (at policy level) in insurance underwriting within the context of climate change?

Direct prevention measures are already an integral part of insurance policies and reflected as such in the underwriting process. There is a real role for these measures in the context of climate change, but not one that could in any way allow to shift the focus away from the need for action, primarily by public authorities, on adaptation, prevention and increasing resilience.

Consider long-term insurance

(para 3.17 to 3.22)

Q9: Do you think that considering long-term insurance contracts (similarly to what is done for life insurance) could help insurers maintain availability and affordability of insurance in light of climate change? Please elaborate on the main pros and the cons for developing multi-year non-life insurance covers.

	Yes
X	No

It is clear from the discussion paper itself that the disadvantages of long-term non-life insurance contracts far outweigh the advantages. The short-term duration of non-life insurance contracts is also envisaged for the protection of consumers. Retail customers are mostly looking for short-term, one-year contracts rather than long-term contracts, as they want to be able to switch between companies. By locking consumers in, these contracts also result in decreased competition between insurers. Such desire for short-term contracts is a general market trend and can also be seen in, for instance, the electricity market. Long-term contracts would also make insurers' situation more fragile from a financial viewpoint, increase the chances of insolvency and negate any potential benefit in terms of insurance availability in the long run.

Such contracts are incompatible with the nature of non-life insurance, which requires a regular re-assessment of risks (including climate-change-related risks) and is often bundled, especially property insurance. There were attempts to have three-year MTPL contracts in some markets which ended in failure for these reasons. Such long-term insurance would require the estimation of such risks in another timeframe than that which is currently envisaged under Solvency II for short-term duration. Finally, this would come with a number of serious operational implications and data issues.

Q10: Do you think that the development of long-term insurance contracts to deal with climate change would require specific regulatory treatment, for example for future premiums?

X	Yes
	No

Given the volatility in, for example, property business, the ability to provision funds and tie losses to a given policy period could create huge run-off liability exposures and the need for substantial capital to be held on account to meet potential liabilities; this would require specific regulatory treatment.

Q11: Do you see potential solutions to the lower flexibility for the insurer and less efficient use of capital as a consequence of long-term non-life insurance contracts?

None specifically.

Q12: In your view, what would be the pros and cons for policyholders if they were offered multi-year contracts?

Here, too, the disadvantages far outweigh any hypothetical advantage. The short-term duration of non-life insurance contracts is first and foremost a consumer protection provision, allowing contractual freedom and competition.

Consider products and services in underwriting strategy contributing to climate change adaptation and mitigation

(para 3.23 to 3.33)

Q13: How could insurers quantify in their underwriting and pricing practices the incentives on the risks insured, and any wider incentives to reduce greenhouse gas emissions?

Quantifying any reduction of GHG emissions as a result of pricing or underwriting is not only too complex, but it also requires data and scientifically proven methods for it to even be feasible. Such prerequisites are hardly available.

Insurers can only measure factors that have an impact on GHG emissions, such as the number of kilometres driven per year to adapt the premium calculation for vehicle insurance. This particular data is available with increased granularity thanks to the development of telematics.

Q14: In which ways could indemnification promote climate resilience by going beyond simple 'like-for-like' replacement of vulnerable properties? Please provide examples (either from real experience or as potential product ideas) and elaborate on the pros and cons to going in this direction.

Many insurers already promote climate resilience through indemnification:

- "Build back better" options in building and content insurance
 - In the Netherlands, greenhouses that were damaged in the 2016 hail event were repaired/rebuilt with tempered glass rather than the original float glass in order to reduce the vulnerability to further hail events.
 - In Belgium, fire insurance offers in cases of total loss, the option for the property to be rebuilt according to the energy-efficiency rules in force at the time, regardless of whether the lost property had such energy efficiency.
- Additional cost clauses in insurance for residential buildings to ensure that special circumstances can be dealt with during repairs and reconstruction.
- Household contents insurance may also include clauses to replace a device that has been destroyed with a more energy-efficient one.
- Circular loss adjustment has become an important instrument used by insurance companies when settling claims by repairing instead of replacing a product.

It should be noted that greener materials may also actually present a higher risk: straw or timber may be greener and lower cost than cement or steel but also have higher fire loads than either of the other less green materials. Any notional saving and increased green credentials may therefore be offset by higher risk and this has to be duly taken into account during the decision-making process.

Potential product ideas include:

- Endorsements on motor insurance policies that allow hybrid replacement: optional coverage whereby, after a total vehicle loss, the insured can replace his or her traditional vehicle with a comparable hybrid vehicle.

- Eco-friendly replacement material endorsements in home insurance, allowing the insured to replace or rebuild with more sustainable materials, practices and products (with due consideration of other risk factors, as explained earlier).

Q15: Are you aware of other insurance products not mentioned in this paper and which would fit with the definition of impact underwriting?

X	Yes
	No

As stated earlier, insurers already practise impact underwriting to an extent; they not only transfer and pool climate-change-related risk, but also contribute to climate-change mitigation and adaptation through the features of their products or their investment strategies.

Examples of such products or product features include:

- Motor insurance policies allowing/encouraging free use of a bicycle during car repairs in Sweden.
- Interpolis green roofs (adaptation) discount on premiums for property insurance in the Netherlands [\[link\]](#).
- Products that support sustainable mobility with a reduced environmental impact (eg, insurance policies for shared vehicles and multimodal mobility).
- Upgrades to green commercial fleets in Germany; products that offer an option to upgrade the company's fleet to hybrid vehicles for new vehicle replacement as part of an endorsement to the policy.

Q16: Are you aware of other insurance services not mentioned in this paper and which could contribute to climate change adaptation or mitigation?

X	Yes
	No

Other insurance services contributing to climate-change adaptation or mitigation include:

- Providing advice and support to policyholders on risk engineering, environmental liability, sustainable building, CO₂ reduction, heat isolation, sensor technology, smart meters, etc.
- Installation of green roofs, solar panels, insulation and even vouchers for climate-adaptative gardens as a service (eg, replacing asbestos-containing roofs with solar panel-equipped roofs).
- Advising municipalities and real estate investors on the risk of (pluvial) flood and heat stress, as well as being an early warning system for extreme weather events.
- Measuring GHG in the claims-handling of buildings to be able to use best techniques, methods and materials when repairing.
- Reviewing entrepreneurs' mileage and vehicle fuel consumption, independently from underwriting or premium considerations.

Q17: Do you have any other comments on the draft Opinion?

On insurers taking climate-change considerations into account:

It is simply incorrect to state that insurers do not include climate-change-related risks in their pricing methodology, as the discussion paper does. Insurers have factored climate-change considerations into their business for a long time. This is based on materiality considerations and happens through the analysis of historical data. This factors in the way climate change makes natural catastrophic events more frequent and more severe over the long-term. Climate-change-related risks are then indeed reflected gradually over time through the annual adjustment of policy terms and conditions (as the paper states, in fact).



While not as straightforward, the future impact of climate change is also already accounted for to an extent, through other means which are all related to the underwriting/pricing process.

Insurers take a holistic view of risk management across their processes and core business, by assessing all risks and their relations to each other, and not focussing on a single risk source insofar as possible. While the risks associated with each insurance contract are considered individually before the contract is concluded, general long-term considerations applicable across a risk portfolio also come into play when deciding the conditions of each contract.

This holistic view has always included prevention measures and it is therefore disappointing to note that the discussion paper seems to imply insurers have yet to really do this. Insurers already actively contribute to climate adaptation by incentivising policyholders to mitigate insured risks via risk-based pricing and contractual terms and by considering measures that contribute to climate-change adaptation or mitigation. This also plays an important role in raising awareness of climate-change-related risks.

The lack of public awareness in long-term land planning is a significant concern: sea levels are expected to rise for many hundred years by several metres, yet governments, authorities and municipalities still allow new buildings close to the sea.

Insurers therefore seek to help policymakers with tools such as risk-zoning and -mapping, land-use planning and building codes, as well as by providing advice to public authorities on projects such as building and maintaining flood defences. Insurers contribute to a better understanding of risk, for example by developing forward-looking risk models. They are updating their risk assessment and underwriting policies to improve how long-term changes in climate are taken into account, often via innovative solutions. This, in turn, helps insurers develop tailor-made products for consumers with different risk profiles.

Finally, insurers' underwriting and pricing practices cannot be considered separately from their role as Europe's largest institutional investor. Through this role, the insurance industry already helps to finance the transition to carbon-neutral, resource-efficient and more sustainable economies.

On mitigation and adaptation:

The discussion paper appears to put mitigation and adaptation on the same level when discussing the role of insurers. The two concepts are different and deserve a better distinction.

As explained earlier, insurers' contribution to adaptation efforts is evident and confirmed by the fact that non-life insurance has been recognised as an activity enabling adaptation to climate change in the EU Taxonomy. Prevention and protection measures have a direct impact on the insured risk as far as climate-related perils are concerned.

The relation between the mitigation of climate change and risk reduction is not as obvious, and further research is needed on the role insurers can play to incentivise policyholders on mitigation, and on the impact on the insured risk.

The discussion paper should therefore have emphasised more the distinction between the mitigation of and adaptation to climate change (eg, paragraph 3.26, which is true for adaptation only, not mitigation).

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