European Insurance and Occupational Pensions Authority

2nd Roundtable on sustainable finance

Summary of the 2nd roundtable discussion organised by the European Insurance and Occupational Pensions Authority (EIOPA) on 23 January 2019 at EIOPA's premises in Frankfurt am Main

On 23 January, EIOPA organised its second roundtable discussion on sustainable finance. Those attending included members of EIOPA's Stakeholder Groups, a representative of the European Commission, consumer representatives, representatives of the insurance and pensions industries, representatives of asset management and rating industries, and representatives of civil society.

In his welcoming remarks, EIOPA's Chairman Gabriel Bernardino reflected on developments since the first Roundtable held in June 2018. To him the time is now to "walk the talk" when it comes to implementing sustainable practices. There is a sense of urgency to act from a societal but also from a business model perspective. Parallel (regulatory) developments should not stand in the way of addressing concrete measures, even in a step-by-step approach.

He mentioned current and upcoming work of EIOPA. To list some: the creation of the EIOPA Catastrophe Expert Network, the development of climate-change related scenarios for future use in stress testing, analysis on the protection gap for natural catastrophes, opinions on ESG (environmental, social and governance) issues in the governance of IORPs, eco-labelling of financial products, and EIOPA's engagement in the European Commission's work on taxonomy.

He commended the engagement of all stakeholders so far and the leadership of the European Commission in addressing sustainability.

While he recognises that integrating sustainability in financial decisions is a challenge, the risk-based framework of Solvency II can cater for this. The insurance industry stands to benefit from assessing sustainability risks on the asset side and, increasingly, on the liabilities side. Being in a business where the long-term matters, it is self-evident that sustainability should matter. This requires leadership at the top level of companies. Acting as stewards for sustainable investments is part of ensuring a gradual transition to a sustainable economy. Consumers will also benefit from this, where product manufacturing and governance requirements integrate policyholder preferences for ESG investments.

Session 1: Consultation on the integration of sustainability risks and factors in Solvency II and the Insurance Distribution Directive

Representatives from industry and civil society gave impulse statements to launch the discussion. The following main points were addressed during the discussion:

- It is important to ensure that the sustainability risk assessment runs consistently and transversally throughout the company. Sustainability adds a third dimension to the insurance business, in addition to return and risk.
- There is a dissonance between the large number of insurers who say they are able to identify financially material climate-related risks for their underwriting and investment portfolios and an equally large number of them who lack a clear investment management policy around climate. Account should be taken of the position of small insurers for whom ascertaining sustainability information about particular assets may be costly.
- A lack of formal escalation processes limits the current impact of shareholder engagement.
- Intermediaries and consumers would benefit from a clear advisory process and more transparency when it comes to explaining why a product would be ESG-compatible. Investing in ESG products is not a black-or-white exercise for consumers: preferences can be taken into account in different ways, depending on the risk appetite, the investment horizon and the portfolio composition of the client. From a distribution perspective, the risk of future liability is a factor.
- Where sustainability risks are taken into account for the sake of protecting the value of the financial product in the long term, this is to the benefit of policyholders. It is important to explain to customers in a balanced way the risks and objectives of investing in environmental, social and governance objectives.
- There were different views expressed on the value added of including sustainability risks and factors in Solvency II and IDD; likewise there were divergent views on how much detail should be provided in any legislation.

Session 2: Looking ahead: Pillar 1 aspects to integrating sustainability in (re)insurers' investments.

Following impulse statements from representatives from industry and supervisory authorities, participants engaged in a discussion on measures for integrating sustainability aspects in quantitative prudential requirements for (re)insurers under Solvency II, following a Call for Opinion from the European Commission. The following main points were raised during the discussion:

- Current industry initiatives aim at integrating ESG criteria in the underwriting process. Industry expects to gain further insight on how these criteria are relevant in assessing the profitability of certain lines of business and, if they would have predictive value.
- Disengagement - in investment or underwriting - from certain economic activities does not happen in isolation but largely follows global market movements.
- Undertakings need to engage with their clients on their respective ESG strategy and performance to ascertain how meet ESG-related underwriting criteria can be met.
- Today's parameters are calibrated to current climate conditions, actuarial approaches are likely backward looking and most models static. The challenge lies in recalibrating them to new climate projections or make them more dynamic, e.g. to reflect transition risk. ESG ratings may be helpful in this respect.

- Long-term climate-related events will impact on non-life and life insurance. For the latter, physical and transition risks will impact on mortality trends.
- It is difficult to know which scenario the market is currently pricing at. Would there be a case for aligning the financial system to a certain (set of) scenarios?
- Different views exist on the treatment of specific asset classes with regard to sustainability risks. From a regulatory perspective the protection of policyholders remains paramount. An evidence-based approach is important.

EIOPA will continue to engage with stakeholders on the topic of integrating sustainability in the (re)insurance and pensions sectors.

As a next step, EIOPA will consider the comments to the Consultation on the Advice on integrating sustainability in Solvency II and the Insurance Distribution Directive, with the aim to submit the final advice to the European Commission in April 2019.

Work will also continue on defining best practices for the integration of sustainability in the underwriting practices, asset and liability valuation and capital requirements of (re)insurance companies under Solvency II, with a view to consult on an Opinion towards the end of Q2 2019.