ShareAction»

Insuring Disaster

Why urgent action is needed to protect the UK's insurance sector

The City is one of the oldest and most important global insurance hubs. It should lead the pack on addressing systemic risks. This includes risks related to environmental and social factors. However, the Climate Change Committee has raised the alarm about the UK's "adaptation deficit", which could pose severe consequences for the insurance industry without urgent Government action[1].

ShareAction's recent survey of 70 of the world's largest insurance companies on responsible investment shows that the industry is not on top of major ESG risks and that the UK's largest insurers could do better.

ShareAction's research paints a troubling picture of the global insurance sector

ShareAction assessed insurers on their internal governance as well as their approach to key systemic ESG issues (climate change, biodiversity loss and human rights). Nearly half (46 per cent) of insurers received an E ranking, representing poor management of material risks and opportunities. Just 16 per cent showed a relatively strong performance in the A and B rating bands. No insurer received the top grades, AA or AAA.

Five out of the 70 global insurers surveyed were UK businesses:

		Rating*	Description for rating band	Rank (Out of 70)
Life & Health	Legal & General Group	A	Strong management of risks and opportunities as well as impacts across multiple themes	1
	Royal London	B	Management of risks and opportunities, building capacity in accounting for impacts across some themes	5
	Prudential Plc	C	Building capacity in management of risks and opportunities across some themes	9
	Phoenix Group Holdings	D	Little evidence to suggest adequate management of material risks and opportunities	15

1. https://www.theccc.org.uk/publication/independent-assessment-of-uk-climate-risk/

With property & casualty business**	Aviva PLC	A	Strong management of risks and opportunities as well as impacts across multiple themes	3

* Top grade possible: AAA
** As there is only one UK firm represented with a P&C business, this briefing does not set out conclusions about this element of our findings in the global industry.

Large UK insurers are not the worst offenders, but standards could be higher

Our results show that large UK insurers often perform better than global peers. However, it is disappointing that no UK insurer achieved the top rating band. Given that these are the largest UK insurers, we recommend that more work is done to understand how smaller UK insurers with less resource are addressing these issues.

ESG issues must not be neglected

It is important that the insurance industry addresses climate change, biodiversity and human rights issues to which it is exposed in order to:

1. **Protect consumers/policyholders:** This includes ensuring that the sector can adapt to the systemic impact of issues like climate change and that individual insurers can provide cover for consumers facing new and changing challenges.

2. **Protect insurance businesses:** Insurance firms that hold assets for a long period may be exposed to increased levels of transition risk arising from climate change, including the risk of stranded assets. This is an issue highlighted in the Government's review of Solvency II[2].

3. **Show global leadership:** Following on from the UK hosting COP26 it is vital the Government leads by example by robustly implementing the TCFD Roadmap and new sustainable disclosure requirements, including for insurance firms.

What we looked at:

ShareAction sent a questionnaire to 70 of the world's largest insurance companies. The survey covered governance, climate change, biodiversity and human rights and looked at both investment and underwriting activities. 47 per cent of the insurers (33 out of 70) either responded directly or agreed to review a prepopulated questionnaire. For the 53 per cent who chose not to participate, we populated their survey response based on publicly available information and invited them to review this.

2. https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/927345/Solvency_II_Call_for_Evidence.pdf

We collected information between November 2020 and February 2021. Our scoring process (including relative weighting of certain topics) is set out in full in pages 8-9 of https://shareaction.org/research-resources/insuring-disaster/

After each insurer was allocated an absolute score, rating bands were calculated relative to peers based on the number of standard deviations from the mean score. Each participant was assigned a rating based on their aggregated score, from AAA through to E. We did not award any AAA or AA ratings, as no insurers were found to demonstrate leading practice throughout their entire approach.

Large UK insurers are embracing TCFD but more needs to be done

The UK is a global leader in supporting uptake of climate reporting against the Taskforce on Climate-related Financial Disclosures' (TCFD) recommended framework (i.e. Governance, Strategy, Risk Management and Metrics & Targets).

The Government recently announced a roadmap to implement mandatory TCFD reporting by UK financial institutions. Some progress has already been made in the insurance industry, but the FCA and PRA will need to work with all insurers to develop best practice across the sector.

Governance: Firms should disclose their governance around climate-related risks and opportunities.

- Three out of five of the UK insurers indicated the board sets the agenda for advancing responsible investment.
- Additionally, the board is involved in responsible investment policy development or approves policies and targets at two firms.

Strategy: Firms should disclose the impacts of climate-related risks and opportunities on their businesses, strategy, and financial planning.

- All but one of the UK-based firms have a climate policy, have made net-zero commitments and have started to report against the TCFD framework.
- This compares with 11 out of 70 insurers globally having made a net-zero commitment and 56 per cent not having started to report in-line with the TCFD recommendations.

Risk management: Firms should disclose how they identify, assess, and manage climate-related risks.

- All UK firms but one have conducted scenario analysis with a variety of scenarios both above and below 2°C.
- While three insurers have investment policies covering coal (both mining and power generation), none have introduced restrictions on investment in conventional oil and gas. The

IEA recently announced that there can be no new oil, gas or coal development if the world is to reach net zero by 2050.

- No insurer has developed a formalised approach to investment in biomass energy.

Metrics and targets: Firms should disclose the metrics and targets they use to assess and manage relevant climate-related risks and opportunities.

- All five firms indicated emissions-related metrics are integrated into their investment processes.
- Notwithstanding the findings around net-zero commitments, only Aviva have additional targets (around funds' allocation to high carbon and low carbon assets).

UK insurers are taking steps as stewards of capital

Economic Secretary to the Treasury, John Glen MP, recently spoke of the UK as a 'world leader in stewardship standards[3]'. These sentiments are reflected in our analysis, which has found UK insurers to be leading the way relative to global peers as stewards of capital.

We found that, in particular, Aviva, Legal and General, and Royal London all engaged across relevant sectors and focussed on climate-related engagement with high carbon sectors. Legal and General and Aviva go further by publishing annual reports which include representative samples of engagement case studies on a wide range of ESG topics, complete with the names of the companies concerned.

Like their global peers, UK insurers are not yet on top of biodiversity loss risks

The HM Treasury-commissioned Dasgupta Review on the Economics of Biodiversity sent a stark message on the global biodiversity crisis we face and outlined the vital role finance will have to play to overcome it. With the Convention on Biological Diversity (COP15) taking place later this year it is essential that the finance sector works to accelerate action to reduce the negative impacts investment has on biodiversity. Our analysis shows that UK insurance firms are not yet on top of this challenge, a finding that is borne out globally.

There are signs of some progress. Our analysis shows that while none of the UK-based insurance firms currently have policies on biodiversity, Aviva and Legal and General had both signed the 'Finance for Biodiversity Pledge'. This commits signatories to engage on biodiversity issues, assess their impact, set targets and report on progress. Aviva and Royal London both said they expected to publish biodiversity policies in the next 12 months.

3. https://www.theia.org/sites/default/files/2020-11/Asset%20Management%20Taskforce_proof7.pdf

UK insurers are weak on human rights risks

Despite initiatives like 2015's Modern Slavery Act and the EU taking strides forward around human rights due diligence, performance by UK insurers on human rights risk was weak. Our research found that, of the five UK firms surveyed, only Aviva has a dedicated policy relating to human rights covering both underwriting and investment activities. This compares with 57 per cent of European insurers, and 27 per cent of insurers globally.

It is concerning that two of the five UK insurers do not have exclusion policies for controversial weapons, which include weapons of mass destruction (e.g. nuclear, chemical and biological weapons) and weapons that cause indiscriminate or excessive harm (e.g. cluster munitions and anti-personnel mines). A number of international conventions prohibit the production, use, and trade of these weapons for states that have ratified these treaties.

At the global level, only 13 per cent of assessed insurers have made a commitment not to invest in companies that are knowingly in breach of human and labour rights, showing that the industry is willing to turn a blind eye to direct and deliberate corporate human rights violations.

There is space for UK leadership in the insurance sector

Despite a mixed performance, relative to their peers UK-based insurance firms performed well. However, the dismal performance by other regions is not a reason for complacency. Almost half of all surveyed insurers were rated 'E' showing a poor performance on material risks and opportunities. The results for US-based insurers were even worse, with 75 per cent receiving an 'E' rating, possibly a result of lack of progress on sustainable finance legislation (a trend that is likely to be reversed under the Biden administration).

In Asia, our research found that Japanese insurers stand out for their performance compared to peers, particularly in China. Despite this, overall performance in the region is poor with only one insurer rated 'B' or above. Given this context, with a relatively mature framework for responsible investment and one of the biggest global markets, there is a real opportunity for UK leadership in the insurance sector.

Policy makers should take action to ensure the UK insurance industry is fit for purpose

Our analysis shows that the UK insurance industry has performed marginally better than global peers, but this should not be used as an excuse by policy makers for inaction. We make several recommendations geared towards enhancing the sector's understanding of ESG risks and boosting its capacity to address them.

4. https://www.gov.uk/government/groups/occupational-pensions-stewardship-council

1. **Government and regulators should promote greater education on ESG and stewardship within the insurance industry** by providing a forum for the exchange of best practice . This could be similar to role the Occupational Pensions Stewardship Council will have in the pensions sector with an initial focus on boosting understanding in the industry of the risks of stranded assets.

2. **Require insurers to consider sustainability factors, including impacts on the environment and society,** when investing and underwriting. In addition, introduce requirements for insurance companies to respond to companies' environmental and human rights due diligence and sustainability reporting.

3. **Introduce greater transparency for insurance companies' underwriting policies relating to ESG factors,** with specific detail required for climate change, human rights and biodiversity.

4. **The FCA should mandate higher standards for investor stewardship.** These should cover environmental and human rights issues.

5. **Fast-track policy changes aimed at addressing biodiversity risk** so that these can be brought in parallel to those related to climate change. This should include a requirement that firms develop a biodiversity policy.

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