SUSTAINABILITY RISKS IN THE INSURANCE SECTOR

ALBERTO CORINTI

Member of the Board of Directors - Italian Insurance Supervisory Authority (IVASS)

Supervisory approach in the light of sustainability risks

Sustainability related events and risks of a disorderly green transition produce potential adverse impacts on both liabilities and assets of insurers. At the same time, the transition to a more sustainable world calls for the insurance industry to be a catalyst in its dual role as risk taker and institutional investor.

From the point of view of supervisors, it is increasingly difficult to separate these two perspectives. A failure to provide a visible and reliable contribution to sustainable factors could affect the value of the company, given its reputational consequences. Strategic risks are more and more affected by the way the company characterizes its sustainability objectives and operations. Also, the correct implementation of the increasingly complex sustainability regulation implies compliance risks that cannot be disregarded.

In this context, the supervisors' traditional objective of consumer protection assumes a broader and more evolved scope. Today, consumer protection must also be seen from the point of view of satisfaction of the protection needs of individuals and of the achievement of sustainability objectives.

How can these goals be pursued in the practical supervisory approach?

First, it is certainly important for supervisors to have deep knowledge of the relevant phenomena and be able to appreciate their risks and opportunities. A prerequisite for any regulatory or supervisory action must be qualitative and quantitative evidence of the phenomena. Today, this appears to be the main challenge.

In 2022 Ivass carried out a survey among the supervised entities, aimed at collecting granular data on the sustainability of the companies' investments and on their underwriting activity in covering natural perils. The companies have given the supervisor highly granular data on a variety of topics, such as the degree of alignment of their investments to the European Taxonomy, the carbon footprint of their portfolio, the premiums collected and the claims paid in the business of providing coverage for natural perils, the role adaptation or preventative measures in the underwriting and pricing of this lines of business.

The path towards sustainability is long and difficult for supervisors too.

This data collection effort has been very challenging for insurers and has even obliged them to use proxies and estimates. This means that there is still a lot to improve for companies in collecting and using data to measure risks, but also for regulators in clarifying the legal framework, introducing widely recognized metrics and facilitating data collection.

But that is not enough. We need that knowledge of these phenomena, and of the potential transmission of the resulting risks and benefits, becomes part of the store of knowledge of those operating at all levels of the Authority. As was the case with the introduction of Solvency II, the new scenario requires an evolution of the supervisory culture. This is often forgotten, yet it is essential but difficult to achieve in practice.

Supervisors, then, must foster awareness of the phenomena by those to whom the insurance service is directed. Insurance education is a fundamental part of supervisory activity, and it is especially so in the current context.

But aside from knowing and ensuring others have knowledge, what are the approaches required from supervisors in the current scenario?

The on-going EU and national regulatory work is intense. New tools and requirements are being developed in the whole regulatory framework: financial requirements, risk management disclosure and market conduct.

In the presence of such new and complex phenomena, supervisors can first of all play an essential role in collecting data and contributing to defining risk metrics and indicators. National authorities and international fora should contribute to the quantitative definition of phenomena and to the identification of ways to measure their risks, even before suggesting how to mitigate them. A lot of work is being done at both EIOPA and IAIS in this area, for example in the development and application of scenarios for climate change stress tests.

Just as for businesses, which are working to integrate ESG measurements into decision-making processes, metrics and indicators related to sustainability risks and opportunities will then need to be incorporated into supervisory processes in order to calibrate their intensity and determine when to intervene on the basis of risk considerations.

The need for a simpler relationship between the Authorities and supervised entities should also be recognised. A simplification of supervisory processes, which are often the unintended result of jumbled and complex regulatory interventions at both the national and European level, would help supervisors and companies to face new challenges without unnecessary burdens.

Overall, the path towards sustainability is long and difficult for supervisors too. It needs to be approached with commitment and perseverance but also with common sense and balance.