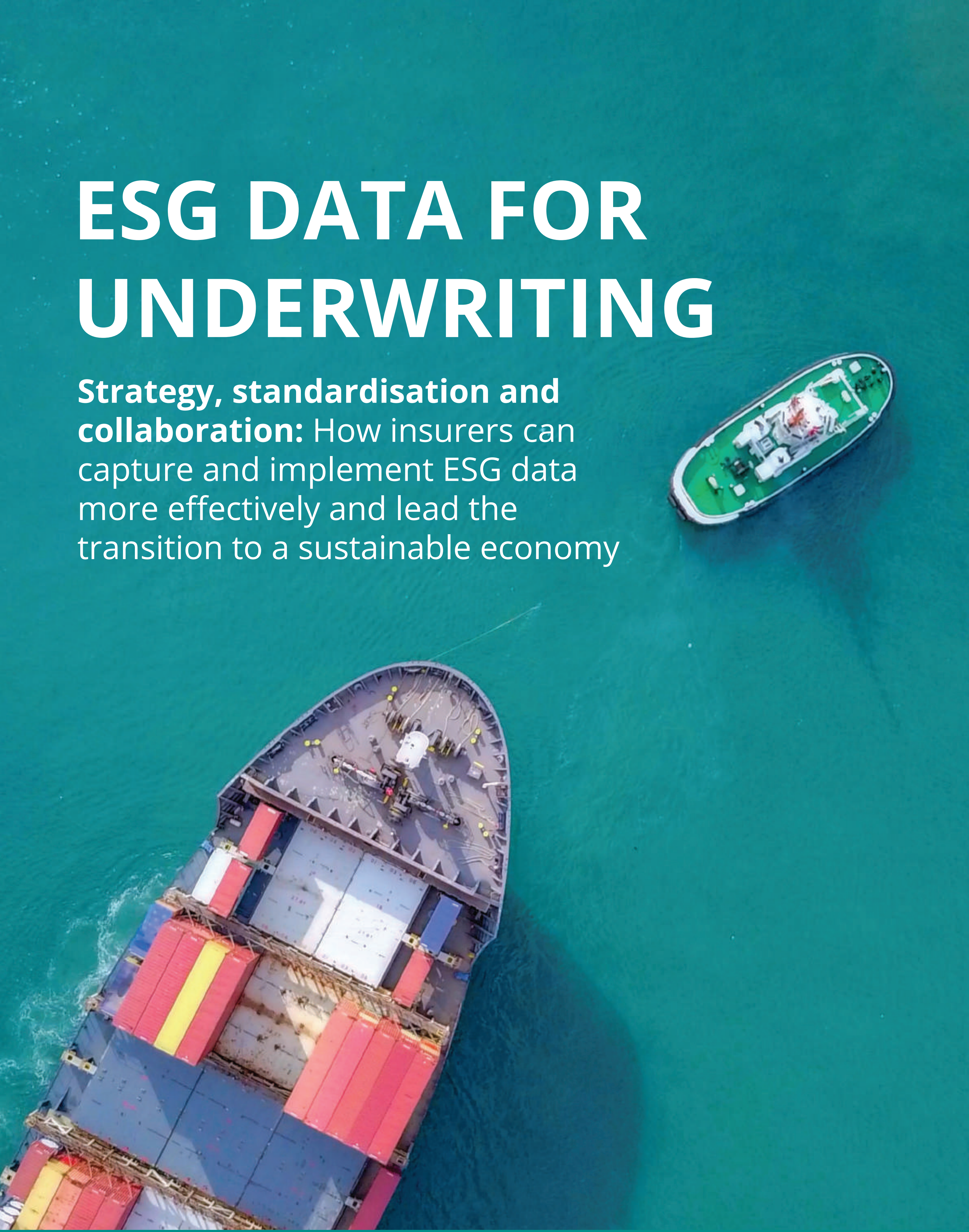

ESG DATA FOR UNDERWRITING

Strategy, standardisation and collaboration: How insurers can capture and implement ESG data more effectively and lead the transition to a sustainable economy

BETTER INSURANCE NETWORK

Oxbow Partners

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Introduction

Better ESG data in the underwriting process is a critical component of (re)insurers' ESG strategies. The industry needs greater consistency and standardisation in how it is captured and how it is used.

ESG is now firmly on the boardroom agenda in the (re)insurance industry. Drivers differ by region and company. Some companies are motivated primarily by increasing regulatory requirements, others by the expectations of stakeholders like employees or shareholders. Some see ESG as a risk management topic whereas others see it as an opportunity to improve underwriting profitability or to drive growth. Senior executives are increasingly driven by a sense of duty to support society in its transition to a more sustainable future.

2022 saw significant progress on ESG in insurance. 30 (re)insurers signed up to the Net-Zero Insurance Alliance (NZIA), numerous companies announced bold underwriting exclusions, insurance-specific disclosure frameworks took shape, and innovative insurance-focused ESG solutions were launched by brokers, rating agencies and data providers.

Navigating this fast-moving landscape is challenge for (re)insurers of all shapes and sizes. Whatever a company's key drivers on ESG, data is a critical enabler of progress.

Many companies are currently trying to quantify the carbon and greenhouse gas (GHG) emissions of their portfolios and associated transition plans. But capturing ESG data is challenging as sources, including disclosure frameworks, are disparate and often not consistent. It is not yet standard practice to request ESG data from insureds and brokers across all lines of business.

Even once (re)insurers have captured information on insureds, they need to work out what to do with it. Is it reliable? What does it mean? Should it affect underwriting decisions? How do we embed it in our underwriting processes and articulate our approach to clients?

Meanwhile, brokers and insureds are demanding greater standardisation of information requested by insurers in the face of a growing administrative burden. They also want more transparency from insurers over how ESG data is being used in the underwriting process.

This report assesses how (re)insurers are tackling these issues and developing their ESG data agendas, their visions for how ESG data should be used in the future, and the crucial role collaboration must play in making progress at both company and industry level.

About this report

Research methodology

This report seeks to assess prevalent approaches being undertaken by commercial insurers and the key challenges they face in capturing ESG data and embedding it in their underwriting processes. In doing so, we also hope to identify action points and best practices that will help insurers derive more value from ESG data and drive efficiency in the market.

(Re)insurers and brokers were invited to take part in our study, along with a selection of key industry stakeholders including industry associations, regulators, rating agencies and representatives of ESG disclosure frameworks. We spoke to 25 organisations in all, including 12 (re)insurers. The research was qualitative in nature, gathered primarily through interviews conducted between August and November 2022. We also held an in-person focus group with nine (re)insurers in London in August 2022.

Questions focused on the approach (re)insurers currently (and intend to) take to capturing and acting upon ESG data on corporate customers in the commercial and speciality (re)insurance underwriting process. Topics included data sources, data quality and reliability, data capture methods, strategic ESG data objectives, implementation into underwriting processes, disclosure frameworks, standardisation and the challenges faced by insurers, brokers and clients. The research did not consider general/personal lines insurers.

Participants' responses were aggregated and analysed by Better Insurance Network with ongoing input from Oxbow Partners. Responses of most (re)insurers have been anonymised as discussions were held under Chatham House Rules. Some interviews were conducted on the record and extracts have been highlighted with the approval of the participants.

Use of this report

This report is written for four main audiences:

- **(Re)insurers:** To help them understand their relative maturity with regards to ESG data and to identify actions which may be necessary given industry norms and best practice.
- **Brokers & clients:** To help them understand the approaches being taken by insurers, the key internal challenges they face in the capture and use of ESG data and to encourage closer collaboration to overcome these challenges.
- **Regulators & policymakers:** To understand the views of (re)insurers and brokers on ESG data, their direction of travel and internal considerations, and to identify areas of uncertainty where further guidance may be required.
- **Trade bodies:** To determine the best way to support the industry given the challenges and objectives identified by participants.

Acknowledgements

Better Insurance Network and Oxbow Partners would like to thank the interviewees from the 25 organisations who participated in the study for their generous time and valuable insights into ESG data which have made this report possible.

Participants

The logos below are organisations that were willing to disclose their participation in the report. This is not an exhaustive list of participants.

Executive Summary

ESG data in context (section 1)

ESG in underwriting is a complex and diverse area covering many often interconnected topics, from greenhouse gas (GHG) emissions and the impact on biodiversity to human rights and labour relations.

The (re)insurance industry is trying to understand what ESG means for its business model and working practices. Drivers differ by region and company (as highlighted in the 2022 Oxbow Partners report, "ESG in Bermuda, the Rising Tide"), and include increasing regulatory reporting requirements, internal and external stakeholder expectations, financial and reputational risk management, enhancing underwriting performance and realising opportunities, and a sense of duty to support the transition to a more sustainable world.

Data is a critical enabler of progress on ESG and a top priority is currently the quantification of carbon and GHG emissions and associated transition plans. However, capturing reliable ESG data is challenging as sources are disparate and often inconsistent. Disclosure frameworks, including TCFD, GFANZ, ISSB, TNFD and others designed to address these challenges, are also inconsistent.

The commitment of the industry to improve ESG data within underwriting is demonstrated through the many pledges and initiatives that have emerged, such as the Principles for Sustainable Insurance, ClimateWise, the Sustainable Markets Initiative and the Net-Zero Insurance Alliance (NZIA).

How insurers capture ESG data (section 2)

Insurers capture ESG data for underwriting in various ways including directly from clients, public sources, and third-party data and ratings providers. It is not yet standard practice to request ESG data from insureds and brokers across all lines of business, and some clients are unable or reluctant to provide it.

It is particularly challenging to get reliable ESG data on small and private companies and there is a lack of visibility into underlying risks in treaty reinsurance and delegated authority business. (Re)insurers have also raised concerns over the reliability and consistency of third-party ESG ratings. Many blind spots exist.

Data capture is also placing a significant burden on underwriters. Where credible data is difficult to source, (re)insurers may rely on sector proxies or assumptions to assess companies and manage their overall ESG risk exposures.

On the other side of the fence, brokers and insureds are demanding greater standardisation of information requested by underwriters as inconsistent question sets are adding to their growing administrative burden. They also want more transparency from (re)insurers over how ESG data is being used in the underwriting process.

Standardisation efforts (section 3)

While there is no simple solution to the challenges outlined in sections 1 and 2, progress is being made in underwriting, including:

- The launch of an insurance-associated GHG emission standard by PCAF and NZIA;
- The development of commercial ESG data solutions including WTW's Climate Transition Pathways and the Moody's/Chaucer ESG Balanced Scorecard;
- Collaborative efforts to standardise question sets in the Lloyd's and company markets; and
- Sector-specific emissions data initiatives like the Poseidon Principles for Marine Insurance.

ESG data implementation (section 4)

Many (re)insurers are capturing ESG data but are unsure how to use it. Some are in the process of embedding ESG data assessment in the underwriting process, though maturity varies significantly between companies and by class of business.

Insurers universally favour supporting their clients' transition plans over the exclusion of companies with poor ESG ratings. But there is a long way to go: ESG data is not yet having a direct influence on underwriting decisions other than blanket exclusions for certain industries such as thermal coal and oil sands. Most (re)insurers are currently trying to quantify and understand ESG impacts at portfolio level rather than using ESG data to penalise or reward individual companies.

However, some (re)insurers we spoke to expect ESG data to influence risk-level underwriting decision-making and pricing within five years. A key enabler will be educating and motivating underwriters to conduct ESG risk assessments.

Improved data quality and standardisation – including automating certain ESG data capture and insight processes – will be critical to supporting this cultural shift.

The need for collaboration (section 5)

Insurers, brokers and reinsurers unanimously agree that greater consistency and transparency can only be achieved through collaboration. They need to speak a common language on ESG.

However, conflicting broker and insurer interests have led to differing opinions on who should lead the ESG data conversation. Reinsurers have to-date been surprisingly passive in driving greater ESG data disclosure. The lack of transparency and consistency in (re)insurers' approaches has also led to a degree of distrust between brokers and carriers, which must be overcome.

Ultimately, all parties have a role to play and need to be more proactive in forming alliances and developing industry best practices.

Next steps for insurers (section 6)

(Re)insurers must develop a coherent ESG data strategy to futureproof their underwriting operations. This involves three steps:

■ Define the ESG data strategy and operating model

Making progress on ESG data will only happen if companies have senior commitment to ESG and a clear ESG strategy on which to anchor their data initiatives. A broader enterprise data strategy could also influence (or be influenced by) ESG data imperatives.

(Re)insurers must therefore identify what their overall ESG strategy implies for ESG data priorities in underwriting – for example, clarity on the objectives of ESG data in supporting underwriting decisions and alignment to guidelines, hypotheses on where the impact is likely to be highest, and target dashboards and metrics.

(Re)insurers must also consider their operating models. Key questions include who will be responsible for the ESG data 'value chain' – from sourcing to testing and integrating into underwriting processes. Leaving responsibility with underwriters risks inaction, whereas pushing centrally risks a lack of impact at the front line.

■ Source relevant ESG data

(Re)insurers must next identify which specific ESG data will allow them to execute on their strategy and achieve the outcomes aligned with their ambition. A company with a net-zero ambition, for example, will require more comprehensive GHG emissions data than a company focused on adhering to the minimum regulatory requirements.

After defining the requirements, the next step is to source data. This will involve assessing data from multiple data providers against a series of metrics that best align to their need, as well as cost, data coverage and reliability. For some (re)insurers, the most appropriate ESG data source(s) may be the same as the source used by the investment function.

■ Execute and embed

Finally, (re)insurers must embed their ESG data strategy into their underwriting function. As ever, this is a mix of technical implementation and cultural transformation, requiring detailed operating model decisions, appropriate technology and relevant governance overlay.

Collaboration with peers, partners and other stakeholders, in partnership with external experts, will often be required to align to best practice and accelerate standardisation.

Whilst the optimal approach may not be possible for all players immediately, setting out a clear ambition, and committing to taking action – even if only in targeted areas – is a must. The direction of travel is clear and (re)insurers will have the ability to deliver more thoughtful and impactful ESG strategies with the right data approach.

The question is not if action is required, but when.

"Insurers must understand what ESG means to them"

Paul Davenport
Finance & Risk Director, Lloyd's Market Association

ESG data has risen quickly up the agenda for Lloyd's insurers. Many have recently defined their goals and approaches to sustainability in response to the rising expectations of shareholders, customers and the public, as well as the Lloyd's Corporation – and data has a vital role to play.

Lloyd's has committed to reach net-zero as a market by 2050 and requested all of its managing agents to establish an ESG framework in 2022. This has been something of a range-finding exercise for the market to understand what is achievable for managing agents and what best practice looks like. For many Lloyd's companies, this was the first time they had attempted to formalise their approach to sustainability and/or ESG.

They should recognise that their strategies aren't the finished article. They will probably need to be reworked in 2023 based on advances made in the past 12 months and as Lloyd's hones its expectations on what these frameworks should contain.

Broadly speaking, a carrier can either define its ESG data strategy around a commercial opportunity or in response to regulatory requirements. Right now, the data landscape is too fragmented to define an evidence-based strategy around a commercial opportunity. The regulatory picture is fragmented too, but regulation is likely to move quicker than the data, so I suspect it will be regulatory reporting pressure driving ESG in the near term.

Many Lloyd's players no doubt aspire to use ESG to identify opportunities and innovate. Once you understand a company's transition plans, you understand their risks, and can begin to think about appropriate products and solutions. We may, for example, see climate litigation carved out of policies as a buyback as we have seen with political and cyber liability risks, with premiums driven by the insured's governance, transition plans and achievements in hitting certain milestones.

However, you need to leverage robust data to support these kinds of innovations. That's why all the progress to date has focused on assessing where we are now rather than identifying and exploring opportunities.

For now, the focus for most insurers is to understand what ESG means to them and what they are going to do with ESG data when they get it. They must then socialise that within their organisations so that, down the line, when underwriters are required to ingest, analyse and make decisions based on ESG data, they have a clear view on the position they should take.

"The market recognises the need for standardisation"

Guy Dormer
Head of Underwriting Strategy, Lloyd's Market Association

Insurers in the Lloyd's market face some unique challenges when it comes to ESG data. Much of the business in the market is syndicated, which puts underwriters one step away from the client and limits their ability to demand information and exert influence.

ESG data is improving and new data sources are emerging all the time. However, the landscape is still extremely fragmented, inconsistent and incomplete. ESG data solutions have often been developed with different objectives in mind, and insurers must work out which data is most appropriate and adapt it to their specific requirements.

The size and complexity of insureds also varies significantly across the market, and data is not easy to obtain on smaller private companies. Some rating agencies have developed solutions to improve coverage of SMEs, but their models still rely heavily on assumptions and proxies, so it's important to recognise the limitations of the data we are working with.

Insureds also want to know what they get in return for providing ESG information. There is, after all, still very little research on the relationship between an organisation's ESG score and its loss performance. This means there is often a gap between what information an insurer wants, what a client can provide and what brokers are willing to push for.

The market recognises we need to move towards a more standardised approach. That in itself is progress. Lloyd's is particularly focused on driving consistency around emissions data and climate impact and Lloyd's carriers are collaborating to develop question sets around these issues – though this isn't as easy as it sounds.

There is some coalescence at a baseline level on emissions data following the launch of PCAF and NZIA's Global GHG Accounting and Reporting Standard for Insurance-Associated Emissions. However, even if we get to a point of consistency in this one focus area, we still face a huge challenge to improve data and incentivise clients in other areas of ESG including transition plans and social and governance factors.

The big brokers, quite understandably, see an opportunity to develop solutions to meet the needs of clients around ESG advice and measurement, and are naturally pushing clients towards their own frameworks. However, competition between brokers and various other agencies with ESG solutions may create a barrier to collaboration and universality.

Going forward, open engagement between insurers and brokers is essential.

"Efficient pricing abhors a data vacuum"

Stephen Weinstein
Former Chair, Bermuda Business Development Agency

The modern Bermuda (re)insurance market has its roots in a wave of innovation and capital formation following Hurricane Andrew, the deadly 1992 storm that caused significant loss of life, material and unexpected financial losses, and the impairment of numerous insurers. Over the succeeding 30 years, firms operating and headquartered in Bermuda have become renowned globally for business practices founded in data acquisition, analytics, and client-focused agility.

Bermuda (re)insurers are committed to meeting their foundational obligations – the fiduciary duty to provide appropriate risk adjusted returns to investors; the contractual and other legal obligations to keep promises made to bondholders, lenders and other creditors; the obligations of transparency and candor owed to regulators and other external stakeholders; and – critically and ultimately – the duty to pay valid insurance and reinsurance claims as promised.

Fulfilling these obligations requires obtaining, analyzing, aggregating, and correlating data: in a word, underwriting. Given the Bermudian (re)insurance industry's distinctive focus on treaty reinsurance, excess insurance, ILS solutions, and other products which distance the (re)insurer from the end client, Bermuda players cannot generally source data including ESG-related data directly and easily from the ultimate insureds. Indeed, this is a challenge for reinsurers globally.

Efficient pricing abhors a data vacuum. Developing – and independent – views on underwriting and data requirements will shape, validate and reinforce reporting and data standards across the value chain, and reinsurers, brokers, insurers and underlying insureds will all benefit from more refined risk understanding. Over time, the arc of market dynamics is toward a degree of standardisation. Bermuda has always been a market where leadership and collaboration come together, and collaboration will continue to define its approach to managing climate-driven risks, navigating social complexity, and enhancing governance.

Reinsurers have a critical role to play in mitigating ESG risks. The world's most difficult challenges are simultaneously our most significant business opportunity. But we must recognise that rapid, material change comes with political, regulatory and culture challenges. The Bermuda market – highly technical, data driven, business-to-business focused, somewhat distant from consumer communications – faces some intrinsic challenges of its own navigating these dynamics.

In my view, most Bermudian reinsurers will rise above these obstacles. The way forward is rooted in a recommitment to core business strategies and value propositions, together with a continuation of candor and transparency appropriate for this era. I am confident the Bermuda culture of meeting policyholder obligations and treating capital providers as business partners will drive it towards leadership in tackling the challenges of ESG data in underwriting.

"We must collaborate on a scale rarely seen"

Nick Dunlop

Managing Director, Client Relationships, WTW

ESG data in the insurance industry is still in its formative stages and much of our industry's understanding of what ESG means can differ. Consistency is noticeably absent, which can cause considerable confusion and be overwhelming for buyers.

Insurers need to agree on some rail tracks along which to operate – what information to demand, which frameworks to align around, what to do with the data and how that impacts clients. Each insurer should of course be allowed some minor differentiation in their approach. However, transparency is paramount: you cannot ask for data and not tell the client what you're going to do with it.

Clients aren't resistant to providing reasonable information when it is contextualised, and I am sure most clients would be interested in receiving some positive differentiation or preferential terms for having better ESG ratings.

However, other than high-level exclusions of high emitting sectors, and some individual insurers taking a lead in offering certain ESG-related benefits, we're not really seeing our industry as a whole vote with their feet yet.

Maybe when there is a more consistent approach to understanding and rating ESG, we will.

As an industry, we understand risk better than anyone else and we have a responsibility and an enormous lever with which to point society along the path of transition. Rather than individual businesses in the market positioning their ESG strategy as a competitive advantage, perhaps we should first focus on collaboration around the metrics and data required. This does mean working together on a scale that is rare to see across the marketplace.

> "Insurers need to agree on some rail tracks along which to operate."

1. ESG data: The insurance context

In summary

- Capturing and embedding ESG data in the underwriting process is becoming increasingly **mission critical** for (re)insurers.
- (Re)insurers are attempting to capture data on a wide range of ESG factors, though measuring **GHG emissions** to enable decarbonisation is the current top priority.
- There are a **range of drivers** underpinning the need to act on ESG data in underwriting: defensive drivers, exploratory drivers and proactive drivers.
- **Defensive** drivers include meeting regulatory requirements, satisfying stakeholder pressure and reputational and financial risk management.
- **Exploratory** drivers include identifying and quantifying which ESG factors are most material to the business, measuring the company's impact on the environment and society, and attempting to draw links between ESG and financial performance.
- **Proactive** drivers include meeting Group and industry sustainability goals, steering society towards a sustainable transition and seizing on new business opportunities.
- An evolving landscape of **disclosure frameworks** has emerged in recent years through which a growing number of large insureds report on ESG factors.
- However, the ESG data landscape remains highly **inconsistent** and **fragmented**.

1.1. What ESG data do insurers capture?

Environmental, social and governance (ESG) is a framework for understanding how companies manage a diverse range of environmental, social and governance risks and opportunities (see table below for a list of some core ESG issues).

(Re)insurers may capture data on a variety of different ESG factors to satisfy their governance policies, ethics and sustainability goals, although in reality they tend to focus on a significantly smaller subset of these metrics.

(Re)insurers address ESG across three core pillars – underwriting, investments and operations. The focus of this report is on underwriting.

(Re)insurers capture ESG data from insureds in the underwriting process to gain a better understanding of how well these companies are addressing ESG issues. By aggregating this data, they can also attempt to measure and address the ESG credentials of their portfolios.

Examples of ESG issues in other industries

Environmental issues	Social issues	Governance issues	Cross-cutting issues
■ Animal mistreatment ■ Impacts on landscapes, ecosystems, and biodiversity ■ Climate change, GHG emissions, and global pollution ■ Local pollution ■ Overuse and wasting of resources ■ Waste issues	■ Child labour ■ Discrimination in employment ■ Forced labour ■ Freedom of association and collective bargaining (i.e. violating workers' rights) ■ Human right abuses, corporate complicity ■ Impacts on communities ■ Local participation issues (i.e. not consulting communities) ■ Occupational health & safety issues ■ Poor employment conditions ■ Social discrimination	■ Anti-competitive practices ■ Corruption, bribery, extortion, money laundering ■ Executive compensation issues ■ Fraud ■ Misleading communication ■ Tax evasion ■ Tax optimization	■ Controversial products & services ■ Products (health & environmental issues) ■ Supply chain issues ■ Violation of international standards ■ Violation of national legislation

Source: RepRisk

1.1.1. Measuring GHG emissions

Whilst measuring and disclosing diversity metrics has been common among (re)insurers for some time, the measurement of greenhouse gas (GHG) emissions has emerged as the main new ESG data focus area for the (re)insurance industry.

Emissions lend themselves relatively well to quantification and are highly pertinent given government decarbonisation commitments, emerging climate-related disclosure policies and green taxonomies, and the (re)insurance industry's intrinsic relationship with climate-related exposures.

The ultimate goal is for (re)insurers to capture data on insureds' scope 1, 2 and 3 emissions. Every companies we spoke to said calculating scope 3 emissions is very complex for their insureds and obtaining comprehensive, reliable data remains a significant challenge (see section 2.4).

Scope 1, 2 and 3 emissions

- **Scope 1 emissions**: Direct GHG emissions that occur from sources owned or controlled by the reporting company (e.g. emissions at their own premises).
- **Scope 2 emissions**: Indirect GHG emissions from the generation of purchased or acquired electricity, steam, heating, or cooling consumed by the reporting company. Scope 2 emissions physically occur at the facility where the electricity, steam, heating, or cooling is generated.
- **Scope 3 emissions**: All other indirect GHG emissions (not included in scope 2) that occur in the value chain of the reporting company. (i.e. upstream production or extraction of purchased materials and downstream emissions that occur as a consequence of using the organisation's products or services).

1.2. Drivers for capturing ESG data

Every (re)insurer has its own unique set of objectives and motivations for capturing ESG data. These can include a combination of defensive, exploratory and proactive drivers.

At this stage, smaller and less mature (re)insurers from an ESG perspective are much more likely to be driven by defensive drivers like regulatory reporting requirements, stakeholder pressure or reputation risk management than a sense of purpose or societal duty.

Of the (re)insurers we spoke to, all were driven by defensive and exploratory drivers to some degree. Some but not all had more proactive motivations.

1.2.1. Defensive drivers

(Re)insurers consider ESG an increasingly important risk that needs to be managed.

1.2.1.1. Regulatory headwinds

Global policymakers are pushing financial institutions towards greater assessment and transparency of their climate-related risks and impacts. For (re)insurers this includes quantifying risks and impacts within their underwriting portfolios.

More than 70 countries have committed to become net-zero economies by 2050.[1] The UK and EU are in the process of implementing related taxonomies which mandate climate-related disclosure and stress-testing.

1. Net-zero commitments must be backed by credible action, UN, 2022

On 5 January 2023, the EU's Corporate Sustainability Reporting Directive (CSRD) entered into force, strengthening ESG reporting rules for large and listed companies and building on the Sustainable Finance Disclosure Regulation (SFDR) for sustainable investment products. The EU also expects large companies to apply new European Sustainability Reporting Standards (ESRS) for the financial year 2024, and listed SMEs by 2026.

The UK launches its Sustainability Disclosure Requirements (SDR) framework for Financial Conduct Authority (FCA) regulated companies by 30 June 2023, though progress on its Green Taxonomy has slowed. In the US, the Securities & Exchange Commission (SEC) proposed rules in March 2022 that would require registrants to include climate-related exposures, including GHG emissions, in their periodic reports and financial statements.[2]

With similar policies percolating in a variety of global jurisdictions, the International Association of Insurance Supervisors (IAIS) stated it intends to promote a "globally consistent supervisory response to climate change" as part of its Strategic Plan, meaning (re)insurers all around the world will face more stringent requirements in the years ahead.[3]

In the UK, for example, the UK Prudential Regulation Authority (PRA) wrote to insurers in January 2022 setting out climate change as one of its top priorities and that it would be incorporate supervision of climate-related financial risks into its core supervisory approach.[4]

1.2.1.2. Political influences

Different jurisdictions have different approaches to ESG and therefore different levels of need to progress on acquiring and using ESG data in underwriting.

In parts of Europe, there is a strong political expectation for all parts of the economy to move towards net-zero with climate change being top-of-agenda for many CEOs. In other parts of the world (e.g. in some states in the USA), there is strong hostility towards embedding ESG into decision making for financial institutions.

(Re)insurers will be influenced by these political factors as they define their ESG data approach.

1.2.1.3. Stakeholder expectations and reputational risk

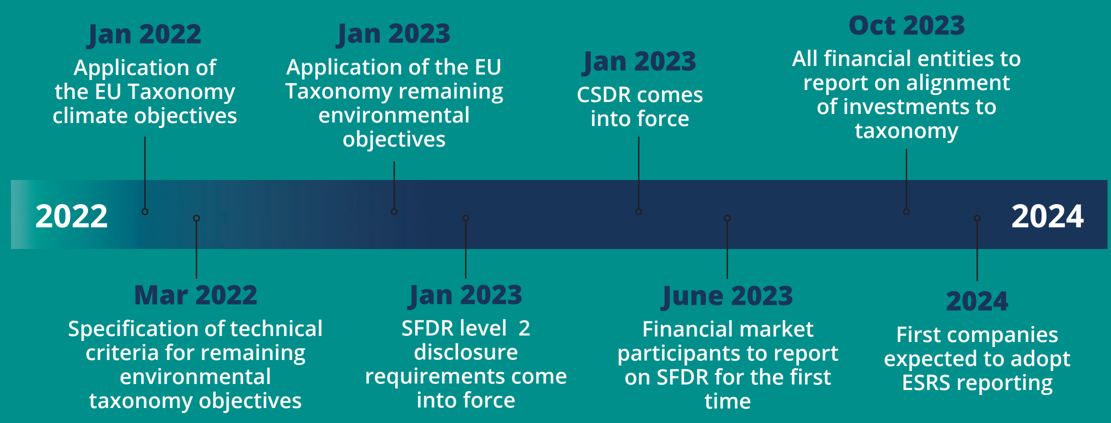
(Re)insurers face rising expectations around business ethics and sustainability from stakeholders including investors, insureds, reinsurers, counterparties, employees and the public. The (re)insurance industry is under particularly intense pressure from activist groups to cut ties with fossil fuel clients. According to Insure our Future, 41 (re)insurers had a coal exit policy and 13 had adopted oil and gas exclusions by October 2022.[5]

2. SEC Proposes Rules to Enhance and Standardize Climate-Related Disclosures for Investors, SEC, 2022
3. Climate risk, International Association of Insurance Supervisors, 2022
4. Insurance Supervision: 2022 Priorities, Bank of England, 2022
5. With new coal uninsurable, insurers start to move on oil and gas, Insure Our Future, 2022

How are regulators driving ESG disclosure?

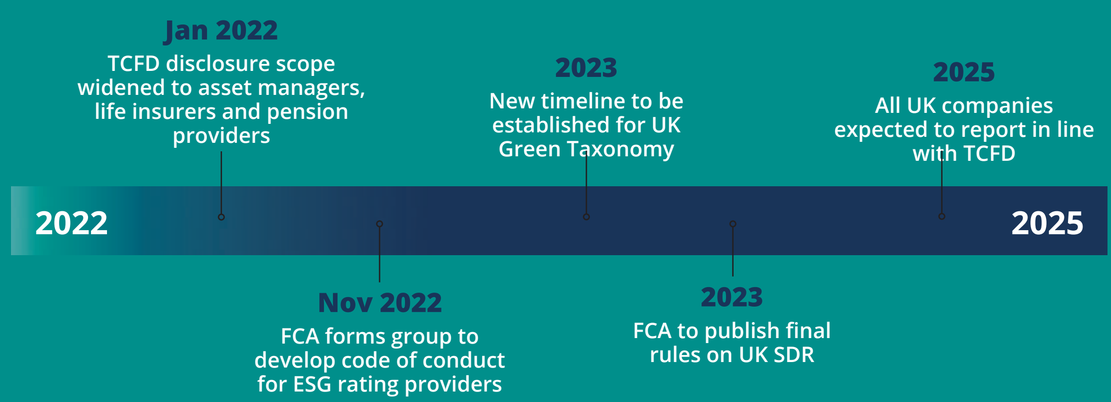
European Union

The EU is generally regarded as the toughest jurisdiction on ESG with a growing body of regulations. This included the EU taxonomy classification system (aimed at preventing greenwashing) and Sustainable Finance Disclosure Regulation (SFDR) concerning environmental impact.



United Kingdom

The UK's FCA and PRA have been following the direction of European regulators with somewhat less stringent measures than SFDR. The UK also requested companies to publish their net-zero plans by the end of 2022 and to align to the Task Force on Climate-Related Financial Disclosures (TCFD) by 2025.



United States

The SEC recently announced plans to expand current reporting to cover areas such as climate impact and diversity.

Source: Oxbow Partners

(Re)insurers we spoke to feel coverage must be phased out gradually to enable an orderly transition. While numerous companies have committed to exclude writing new business in these sectors, none have cut ties altogether. The need to maintain relationships with existing fossil fuel clients for potentially decades more poses an ongoing reputational risk.

Fossil fuels aside, providing coverage to companies exposed for unethical practices, human rights abuses, environmental negligence and other controversies can damage (re)insurers' reputations. Accusations of greenwashing or misleading investors or customers over sustainability credentials is another reputational risk which may also incur fines.

(Re)insurers must therefore capture reliable data to accurately assess and represent the ESG credentials of their underwriting portfolios.

1.2.1.4. Alignment with disclosure frameworks

An increasing number of (re)insurers are signatories of one or more climate-related disclosure frameworks, through which they report on their own emissions and other ESG factors (see section 1.4 for further detail). This includes disclosing the risks and impacts within their underwriting portfolios, requiring them to capture and aggregate data from underlying insureds.

1.2.2. Exploratory drivers

(Re)insurers increasingly want to leverage ESG data to understand the impact they have on the environment and society through their operations and supply chains and the activities they finance via their investments and underwriting.

Depending on their sustainability objectives, the findings may enable them to identify ESG risk and materiality hotspots within their portfolios, focus client engagement efforts to improve ESG credentials or steer capacity towards more sustainable areas of the economy.

Several (re)insurers told us they are also in the process of investigating the correlation between ESG factors and loss performance which may eventually enable them to link insureds' ESG credentials to capacity, terms and pricing (see section 4.2).

1.2.3. Proactive drivers

Some (re)insurers believe they have a duty to use their unique influence as investors and underwriters in the real economy to steer clients – and society – towards a greener, fairer, more sustainable future. This can be achieved by:

- Underwriting sustainable sectors of the economy;
- Building resilience through risk mitigation and adaptation;
- Implementing underwriting exclusions for bad ESG risks; and
- Engaging with clients to improve behaviours.

The transition to a more sustainable, low carbon economy also potentially represents a huge financial opportunity for the (re)insurance industry. (Re) insurers may therefore increasingly leverage ESG data to identify growth opportunities and develop new products and solutions.

Key opportunities for the (re)insurance industry include:

- Underwriting the growing renewables sector;
- Developing coverage for carbon capture, secondary carbon markets and emerging green technologies;
- Closing the protection gap through affordable solutions;
- Climate risk modelling and scenario-testing solutions; and
- Risk mitigation solutions.

Proactive (re)insurers usually publish a sustainability strategy which sets out their purpose, often aligned with broader industry sustainability goals and principles (see section 1.3).

In many cases, particularly among smaller (re)insurers with less ESG maturity, being a force for good in society is a lower priority than traditional business objectives like profitability.

While several of the sustainability leaders we spoke to felt empowered by their companies' sense of purpose, some felt their corporate culture could create barriers to embedding ESG data in the underwriting process.

“At some point, short-sighted insurers writing high carbon intensity sectors will have to radically change, whether forced by regulation or other factors.”

– Ben Howarth, ABI

“As an industry, we have a responsibility and an enormous lever with which to point society along the path of transition.”

– Nick Dunlop, WTW

1.3. Insurance industry sustainability principles

Many leading (re)insurers are signatories of one or more sets of industry-specific sustainability principles. Capturing and embedding ESG data in underwriting is often a key component of executing on these commitments. Three prominent initiatives are outlined below.

1.3.1. UNEP FI Principles for Sustainable Insurance (PSI)

Launched by the UN in 2012, the PSI serve as a global framework for the insurance industry to address ESG risks and opportunities.[6] The PSI has 138 signatories and 99 supporting institutions, representing 33% of global premiums. The principles include commitments to:

- Establish processes to identify and assess ESG issues inherent in underwriting portfolios;
- Be aware of potential ESG-related consequences of the company's transactions;
- Integrate ESG issues into underwriting decision-making processes;
- Develop products and services which have a positive impact on ESG issues;
- Assess, measure and monitor the company's progress in managing ESG issues;
- Proactively and regularly disclose this information publicly; and
- Participate in relevant disclosure or reporting frameworks.

1.3.2. Net-Zero Insurance Alliance (NZIA)

The UN-convened NZIA is a group of (re)insurers which has committed to transition their underwriting portfolios to net-zero GHG emissions by 2050, consistent with a maximum temperature rise of 1.5°C above pre-industrial levels by 2100.[7] Established in 2021, the NZIA had 29 signatories representing over 14% of global premium volume at the time of writing.

The NZIA includes a workstream focused on developing consistent metrics and targets. In January 2023, it launched its Target Setting Protocol to help members set their first interim science-based targets to align underwriting portfolios with a 1.5°C transition pathway. The NZIA also collaborated with the Partnership for Carbon Accounting Financials (PCAF) to launch the first global standard for measuring and disclosing insurance-associated GHG emissions in November 2022 (see section 3.1).

1.3.3. ClimateWise

ClimateWise is a convening body formed in 2007 to align the (re)insurance industry in its response to climate-related risks and opportunities.[8] At the time of writing, at least 40 (re)insurers and brokers were signatories to the ClimateWise Principles. Commitments include:

- Incorporate climate-related issues into strategies and investments.
- Lead in the identification, understanding and management of climate risk.
- Reduce the environmental impact of business.
- Enhance reporting.

6. Principles for Sustainable Insurance, UNEP FI
7. Net-Zero Insurance Alliance, UNEP FI
8. ClimateWise, Cambridge Institute for Sustainability Leadership

1.4. ESG-focused disclosure frameworks

A proliferation of disclosure frameworks has emerged in the past two decades designed to bring consistency to the way corporations measure and report on climate-related issues including GHG emissions. While there has been some consolidation of frameworks in recent years, the landscape remains an 'alphabet soup' of acronyms.

Key incumbent and emerging initiatives include:

- **The Global Reporting Initiative (GRI)** – formed in 1997, the GRI creates a common language for organisations to report their impacts across a range of sustainability issues;
- **The Task Force on Climate-Related Financial Disclosures (TCFD)** – created by the Financial Stability Board in 2015 as a framework for companies to assess and disclose climate-related risks. TCFD reporting is being made mandatory for all UK companies in 2025;
- **The International Sustainability Standards Board (ISSB)** – launched at 2021's COP26 by the IFRS Foundation, the ISSB is developing global baseline of company sustainability and climate related disclosure standards, including scope 3 emissions, for release in 2023; and
- **The Task Force on Nature-Related Financial Disclosures (TNFD)** – an emerging framework focused on identification, assessment, metrics and disclosure relating to companies' nature-related risks including impact on biodiversity and ecosystems. TNFD releases v0.4 of its beta framework in March 2023 with the aim of launching v1.0 of the TNFD Framework in September 2023 (see section 2.4).

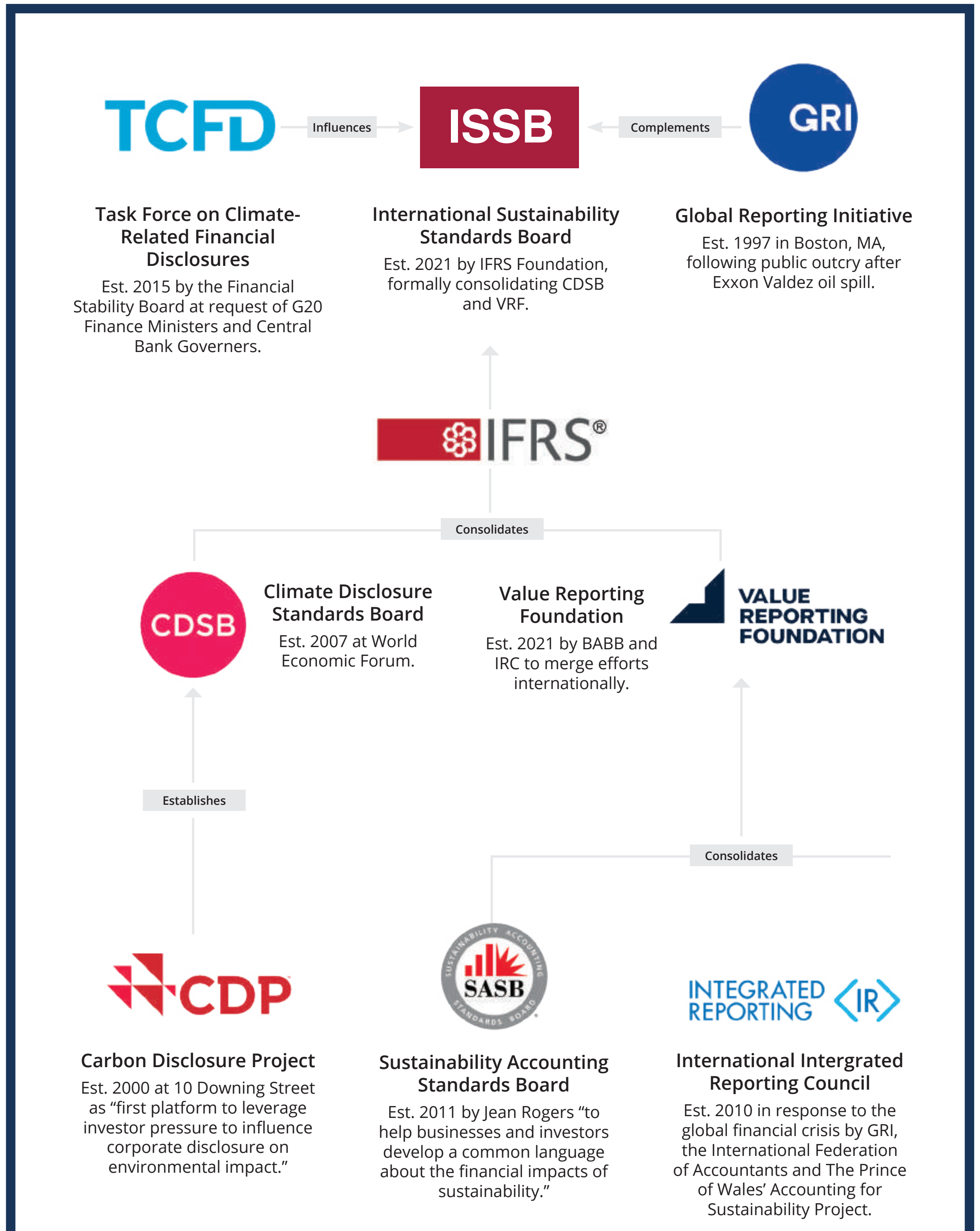
While these frameworks help (re)insurers to capture data from participating insureds in a consistent format, (re)insurers must still navigate a highly inconsistent and fragmented client reporting landscape.

Participation in these frameworks is skewed towards large public corporations and huge portions of the insured company universe – particularly in the private sector – do not follow their recommendations.

Even among larger listed companies there is reporting inconsistency. TCFD said in its 2022 status report, for example, that while 80% of large companies disclosed in line with at least one of its 11 recommended disclosures, only 4% disclosed in line with all 11 and only around 40% disclosed in line with at least five.[9]

9. TCFD 2022 Status Report, TCFD, 2022

Evolution of prevalent disclosure frameworks



Source: Auditboard

> “I'd rather insurers get climate information directly from the insured rather than buying this data from rating agencies and data providers. Insureds should be able to control their own narrative by providing the information.”
>
> *– Amy Barnes, Marsh*

> “We only ask clients for ESG data when it's not publicly available.”
>
> *– Insurer*

> “We know from producing our own sustainability report how much effort is required to collect and report ESG data. I can see how a large cap can do this but for SMEs this is very demanding.”
>
> *– Reinsurer*

2. Capturing ESG data

In summary

- Insurers capture ESG data in a variety of ways, both **directly from clients** and from **external sources** such as public records and third-party providers.
- Many engage **rating agencies** or specialist **ESG data providers** to generate ESG risk ratings/scores for clients and sectors.
- Asking insureds and brokers to provide relevant information is **not yet universal practice** across all lines of business.
- Larger insurers with more resources may deploy a combination of approaches, aggregate data and develop their own **ESG rating methodologies** to generate proprietary risk scores.
- Where credible data is difficult to come by, insurers may rely on **sector proxies** or **assumptions** to assess companies and manage their overall ESG risk exposures.
- Many **blind spots** and inconsistencies exist in the ESG data landscape.
- Inconsistency in insurers' approaches causes significant **administrative burden** for insureds and their brokers.
- Capturing data **manually** also places additional burden on underwriters.
- Brokers and insureds would welcome **standardisation** of insurer **question sets** and greater **transparency** over how their ESG data is being used.

2.1. Client questionnaires

The most direct way of gathering relevant data on a company's ESG credentials is to ask them for it. This is the best way for an insurer to capture up-to-date information, tailored to the topics and metrics it deems relevant and presented in a format of its choosing.

However, this creates an additional burden for the client and/or its broker, so some insurers prefer to source information from external sources before asking clients directly.

Most of the insurers we spoke to engage clients directly on ESG in at least some classes of business – typically those deemed more sensitive to ESG issues such as carbon emissions. This usually involves providing a questionnaire as part of the submission process.

None of the insurers we interviewed include ESG questions in the submission process across their entire books of business yet, though several plan to create core question sets that can be rolled out and adapted across multiple classes of business.

Direct engagement is particularly valuable when assessing private and smaller companies as there will be no public disclosures to fall back on, and these companies are less likely to fall under the scope of rating agencies and ESG data providers.

2.1.1. Question types

The sophistication of insurer question sets varies significantly depending on where the insurer is on its own ESG maturity curve.

Questions range in complexity from simple Yes/No questions to assess a company's general approach to ESG, to quantitative examinations of KPIs and targets.

Examples of qualitative questions:

- Do you have a dedicated ESG committee?
- Is board remuneration linked to carbon emission reduction?
- Do you have a climate transition plan?
- Do you test on animals?

Examples of quantitative questions:

- What were your Scope 1 & 2 GHG emissions in 2022? (K tons CO_2e)
- What reduction in GHG emissions are you targeting by 2030? (K tons CO_2e)
- Provide a breakdown of the ethnic diversity of your senior management team.

2.1.2. Resistance and inaccuracies

Insurers told us they are wary of burdening clients and brokers with too many questions.

Clients may be resistant to doing extra work or sharing ESG information – particularly if they believe it may inadvertently harm their ability to obtain coverage or if clarity is lacking over how the insurer intends to use the data and whether it could directly affect insurance terms.

Data disclosed may also not always be reliable. One insurer told us they look for external validation where possible, including membership of industry accreditation schemes which provide assurances that clients adhere to rules on issues like pollution and human rights.

2.1.3. Climate transition plans

While most of the insurers we spoke to consider client climate transition plans equally as important as current emissions, the assessment process is nascent.

> “Even with self-reported data, there can be data accuracy problems.”
>
> *– Broker*

> “What information can underwriters legitimately ask for if it is not informing underwriting risk?... It's not my job as a broker to embolden insurers and make the underwriting process more complex for clients.”
>
> *– Amy Barnes, Marsh*

> “Without a client questionnaire, it's very difficult to know whether an insured has a transition plan that will meaningfully get them to net-zero. Driving consistency in question sets is a pressing need.”
>
> *– Reinsurer*

> Rather than asking simple questions like 'do you have a net-zero strategy?' and 'is it tied to board compensation?', carriers are now asking clients where they are on their transition trajectories and where they plan to be by 2030 or 2050. It's becoming a much more sophisticated and complex process.
>
> *– Broker*

> A transition plan should translate ambitious strategic objectives into concrete steps to be taken in the short and medium-term.
>
> *– UK Transition Plan Task Force*

Assessment of transition plans – if done at all – is largely qualitative in nature. Historical company emissions data is limited and many companies are still implementing their first formal climate transition plans, so it is too early to assess their progress or trajectory.

According to 2021 research by CDP and Oliver Wyman, only 19% of insurers assess whether clients are aligned to a 'well below 2°C world', and just 14% encourage their clients to set SBTs (asset managers are roughly four times more likely to do so).[10]

However, the insurers that do ask questions appear to be getting more prescriptive, asking clients to reveal near, medium and long-term targets. Meanwhile, WTW's Climate Transition Pathways initiative is attempting to standardise transition plan disclosure for insureds (see section 3.4).

As updated emissions data is provided at each renewal it will become easier to assess the feasibility of companies' targets and benchmark progress against peers using sector data. For now, insurers are likely to be satisfied to simply to know a plan is in place, even if there is little accountability.

UK formalises transition plan disclosures

At COP26 in 2021, the UK announced it will mandate listed companies and financial institutions to disclose their net-zero transition plans.

In April 2022, it launched the UK Transition Plan Taskforce, co-chaired by Aviva CEO Amanda Blanc, to help companies in the private sector to create robust transition plans.[11]

As well as bringing consistency to transition plan disclosures, the framework may help insurers when designing their own assessment processes.

In November 2022, the UK published a new Disclosure Framework and implementation guidance for public consultation.[12]

The framework is built around three guiding principles:

- **"Ambition"** – Outline ambitious plans to contribute to and prepare for a rapid and orderly economy-wide net zero transition, focusing on direct abatement across scopes 1, 2 and 3.
- **"Action"** – Focus on concrete actions which emphasise the short-term and strive for resilience.
- **"Accountability"** – Deliver the plan through clear governance mechanisms and consistent, comparable and decision-useful reporting and verification.

10. Now for Nature, CDP/Oliver Wyman, 2022
11. Consultation, The Transitional Plan Taskforce Disclosure Framework, TPT, 2022
12. Consultation, The Transitional Plan Taskforce Implementation Guidance, TPT, 2022

2.1.3.1 Offshore energy transition plan questionnaire

In December 2021, the Lloyd's Market Association Joint Natural Resources Committee (JNRC), which serves the interests of insurers writing offshore energy risks in London, published a Transition Questionnaire (JR2021-033) to help managing agents collect information relating to their clients' progress on energy transition, sustainability and ESG.[13]

Most of the questions are generic in nature and could be applied to any class of business.

JNRC Transition Questionnaire for offshore energy clients

01. Has your company scientifically measured your greenhouse gas emissions for your scope 1, 2 and 3 activities? Please include some brief details.
02. Do you have an evidence-based plan to reduce scope 1 greenhouse gas emissions? Please attach.
03. What operational performance benchmarks do you currently use to track greenhouse gas emissions and progress to reduce them?
04. Which metric do you intend to use to assess your transition progress?
05. Have you engaged with an independent third party to assist and verify your transition process?
06. Is your plan aligned with the Paris Agreement? If not, please give further details.
07. What transition milestones have you identified in your plan?
08. Has your timeline changed since you first started this process?
09. Do you have an allocated budget for transition? What is this as a percentage of your CAPEX?
10. Do you have a nominated board member responsible for transition progress and is it an ongoing agenda item for board meetings?
11. Is your company strategy aligned with your transition goals?
12. Can you provide some narrative around your progress to date? Please include any other relevant information, including your ESG framework as applicable.

Source: Lloyd's Market Association

2.1.4. Unstructured risk data

In some cases, ESG data may be captured as a matter of course during the risk assessment and underwriting process. One insurer gave an example of a large infrastructure project including an environmental impact assessment report in its submission pack, giving the insurer a good sense of whether the project should be flagged as a potential ESG risk.

This data will often be unstructured, sitting within PDF documents, for example, requiring manual discovery and analysis in the underwriting assessment process.

13. Joint Natural Resources Committee circulars, Lloyd's Market Association, 2022

> “There are hundreds of questions we could ask within ESG, which is too many. Maybe we can get that down to five or ten which become standards within the industry.”
>
> *– Insurer*

> “Clients aren’t resistant to providing reasonable information when it is contextualised.”
>
> *– Nick Dunlop, WTW*

> “Many clients in carbon intensive industries are fearful of the disclosures they’re being asked to make because they think it could result in an automatic prohibition.”
>
> *– Amy Barnes, Marsh*

2.1.5. Calls for standardisation

Brokers and insureds are growing frustrated by the lack of consistency in approaches shown by insurers when it comes to capturing ESG data.

Every insurer considers ESG materiality in its own way, meaning the substance and format of question sets and the metrics insurance buyers are expected to share can vary wildly.

Fielding different questions in a variety of formats from multiple insurers can become a serious drain on resources, particularly for smaller firms or companies with complex insurance programmes.

An insurer must therefore weigh the benefits of getting a fuller understanding of their client’s ESG profile with the potential impact on the client relationship. This may mean prioritising a handful of key metrics and limiting the number of questions asked.

Several brokers also expressed frustration at the lack of transparency over insurers’ methodologies – in other words, how the ESG information being requested is being used and whether this will have a material impact on pricing, terms or limits.

Several insurers admitted even they do not yet fully know the answer.

Insurers agreed that, at present, ESG data in its own right is not seen as competitively sensitive, and that competitive value is more likely derived from what they do with that data (explored in section 5).

There is a strong consensus among brokers and insurers that the industry must align around a common set of core questions and standardised metrics.

While there can be no ‘one size fits all’ questionnaire for ESG risk assessment, the practitioners we spoke to felt there are certain common questions that could have broad applications, with underwriters able to tailor additional questions by class or sector.

Several insurance industry data initiatives have been set in motion to this end (see section 3).

2.2 Publicly available information

Publicly available information such as public filings and government records is often the first port of call for insurers when assessing client ESG credentials.

This information is usually captured manually by underwriters during the assessment process, though several insurers expect this kind of information to eventually find its way into underwriter dashboards in the years ahead, just like other risk data do today.

While it is possible to find relevant ESG information on most publicly listed companies and very large private organisations, there may be little or no data in the public domain for recently listed organisations and large swathes of the private sector, especially SMEs.

Some common public sources of ESG data used by insurers are outlined below.

2.2.1. Corporate filings

Many large public companies include ESG information in their annual filings and climate-related disclosures are now mandatory in a growing number of jurisdictions (see section 1.1).

A growing number of firms have committed to report emissions data in a standardised format through recognised frameworks like TCFD. However, the data landscape is still extremely inconsistent in scope, substance and format.

The level of detail included in filings varies significantly depending on where a company is on its ESG maturity curve, which ESG factors it considers important and the regulatory environment in which it operates.

2.2.2. Company sustainability reports & websites

Annual ESG or sustainability reports also come in many guises but can provide insurers with valuable insights. According to McKinsey, more than 90% of S&P 500 companies now publish ESG reports in some form, as do approximately 70% of Russell 1000 firms.[14]

Reports vary in sophistication but do provide a window into a company’s approach to ESG.

Insurers use these reports to establish, for example, whether a company links board remuneration to ESG KPIs or whether there are emissions or DEI commitments in place.

More sophisticated reports may include science-based targets and quantitative metrics illustrating how a company is advancing on a variety of topics, from GHG emissions to DEI.

In the absence of a publication, company websites may also give insurers some basic information on ESG approach and a sense of how seriously the firm takes ESG.

14. Does ESG really matter – and why? McKinsey & Company, 2022

2.2.3. Industry associations/governing bodies

Some industry associations publish emissions data captured from member companies which can help insurers develop sector proxies from which to base internal calculations and benchmark clients.

One example is the International Maritime Organization (IMO), which curates the IMO Ship Fuel Oil Consumption Database[15] and releases an annual Greenhouse Gas Study[16].

Ships of 5,000 gross tonnage and above are required to collect consumption data for each type of fuel oil they use, as well as other data including proxies for transport work. They report this data annually to their flag states, which report back to the IMO.

Another is the International Air Transport Association's (IATA) CO_2 Connect emissions calculator based on airline data.[17]

2.2.4. Insurers challenged by a fragmented data landscape

A key limitation with each of the afforementioned data sources is the timeliness of the data, as it will usually refer to the prior financial year and may not be promptly updated.

Public data is inconsistent in format and scope, often unstructured and not designed for use by insurers, making the research process laborious and the resulting datasets difficult to manage efficiently. More importantly, it doesn't always provide underwriters with the answers they need.

2.2.5 Social media, media and other sources

ESG-related data (e.g. emerging controversies) can be captured from social media posts, blogs, news websites and traditional prinat and broadcast media outlets. AI enables data specialists to capture much of this information automatically using ESG-related keywords.

Other sources include research companies, NGOs, think tanks and government agencies.

2.2.5 Greenwashing an ever-present threat

Companies tend to focus on their strengths and gloss over their weaknesses when communicating publicly. In the worst cases this can manifest as outright 'greenwashing'.

High-profile lawsuits and penalties for alleged greenwashing provide a growing deterrent. However, underwriters must validate and verify information and be able to spot red flags.

Failing in this exposes insurers to regulatory, reputational and financial risks of their own.

15. Data collection system for fuel oil consumption of ships, IMO, 2023
16. Fourth Greenhouse Gas Study 2020, IMO, 2023
17. IATA CO2 Connect, IATA

2.3. Third-party data providers

Insurers with sufficient budget often engage specialist providers of ESG data and ratings.

2.3.1. Rating agencies

Rating agencies provide ESG ratings or scores for thousands of individual companies. This provides an important service for insurers seeking to understand those companies' ESG profiles and risks.

Most of the insurers we interviewed use ESG ratings as a guide and supplement the ratings with their own proprietary research. However, insurers with limited resources dedicated to ESG research and assessment may rely entirely on these ratings.

While rating agencies can provide an ESG rating with a high degree of confidence for most large publicly traded companies, coverage of private companies is limited. However, rating agencies' scope of coverage is slowly improving.

Rating methodologies vary significantly between providers. Two insurance companies we spoke to conducted studies which put the correlation between different rating agencies' ESG ratings as low as 30%. An insurer's choice of rating partner can therefore make a big difference to its perception of any given company's ESG risk.

2.3.2. Rating agencies' increasing role… and scrutiny

Several insurers suggested to us that rating agencies could have an important role to play in developing a central repository of consistent ESG ratings – though they have some reservations about the reliability of the ratings currently being provided (see section 2.3.3).

Rating agencies face increasing scrutiny from global regulators. In November 2021, the International Organization of Securities Commissions (IOSCO) published set of recommendations for regulators and ESG rating providers covering issues of transparency, good governance, management of conflicts of interest, and systems and controls.[18.]

In November 2022, the UK Financial Conduct Authority formed a working group to develop a formal code of conduct for ESG data and ratings providers, having previously said it plans to bring more consistency, reliability and accountability to ESG ratings.[19.]

18. ESG Ratings and Data Products Providers, Final Report, IOSC, 2021
19. Code of Conduct for ESG data and ratings providers, FCA, 2022

> "Ratings agencies, given their position within the market and the wealth of data that they offer, are well placed to collate information on ESG practices by companies. It would be difficult for an independent agency or governmental organisation to adopt this role."
>
> *– Rating agency*

> "If a rating agency could develop a rating that was accepted globally in the same way their credit ratings are, that would be a great solution."
>
> *– Broker*

> "We conducted a study and found a correlation of only around 30% between different agencies' ESG ratings."
>
> *– Insurer*

> Consistent ESG ratings from an organisation with enormous credibility would be very beneficial and some great rating agencies are starting to rise to the challenge. However, we don't want a cottage industry for ESG ratings which will not be helpful to anybody.
>
> *– Nick Dunlop, WTW*

> All rating providers have their pros and cons. It is important to understand their methodologies, what they are trying to demonstrate – and not – with their ratings, then determine what information is valuable for specific use cases.
>
> *– Insurer*

Rating agency approaches

Moody's

Moody's ESG Solutions scoring is divided into two categories:

- Issuer Profile Score (IPS)
- Credit Impact Score (CIS)

IPSs are separate environmental, social and governance scores that assess an entity's exposure to ESG risks. CISs reflect the impact of ESG considerations on the credit rating of an entity. Both scores use a five-point scale. Moody's in 2022 developed a data driven ESG scorecard in partnership with global specialty (re)insurer, Chaucer.

S&P

S&P Global Ratings ESG Evaluation Reports are based on two inputs:

- ESG Profile Score
- Preparedness Opinion

The ESG Profile Score summarises the current and near-term effectiveness of the entity's ability to manage ESG risk exposure and uncover ESG opportunities relative to peers. The Preparedness Opinion is a qualitative view of an entity's capacity to anticipate and adapt to long-term disruptions. The evaluation is a single score on a 100-point scale.

Fitch

Fitch Ratings offers ESG Relevance Scores to support credit decision making. Each entity is assessed using one of 100 sector-specific templates. Within the template, 15 subfactors are scored individually on a scale of one to five, with higher scores indicating greater materiality to the credit decision. The results feed into an overall ESG Score alongside individual Environmental, Social, and Governance scores.

AM Best

AM Best considers Environmental, Social and Governance factors as part of its credit rating for (re)insurers. In rating analysis, AM Best considers ESG factors only if they are believed to have an impact on financial strength within a time horizon, usually 36 months.

Source: Oxbow Partners

2.3.3. ESG ratings not yet fully trusted by insurers

Several insurers we spoke to have reservations over the reliability of ESG ratings in their current form, even though many of those firms also use ratings in their assessments.

ESG risk rating methodologies are often opaque, giving insurers limited look-through to underlying metrics. Insurers also said it was not clear how rating agencies weight different ESG factors and how, if at all, transition plans and targets will be factored into their rating calculations going forward.

They also said it is difficult to independently verify the quality, reliability or timeliness of data being provided to the agencies, which could be based on prior year disclosures.

As well as choosing a highly reputable, trusted rating partner, one insurer recommended using historical ESG ratings to back-test the reliability of agency/provider methodologies. Another suggested conducting a comparison of how different providers present the same publicly available information.

Insurer concerns over ESG ratings

- Concerns over the 'black box' nature of rating methodologies.
- Lack of correlation between different rating providers' scores.
- The vulnerability of ratings to being based on outdated information.
- The use of sector proxies, particularly when rating private companies.
- Ratings do not yet typically consider transition plans.

> Your conversations with rating agencies about your own ESG scores provide a window into how much you should trust the data they provide at the front end.
>
> *– Insurer*

> We've worked with a number major ESG providers and their scoring doesn't correlate nearly as highly as you would expect. There are plenty of contradictions.
>
> *– Insurer*

> We are passionate about delivering the highest possible degree of accuracy, timeliness, and completeness in our corporate, market and financial information. We challenge our clients to tell us when we've missed the mark and reward customers who report quality issues.
>
> *– Raphael Zindi, S&P*

“Ratings are a first step”

Laura Wanlass
Global Corporate Governance & ESG Advisory Practice Leader, Aon Human Capital Solutions

It is very challenging for insurers to truly gauge a company’s ESG risks and opportunities at this point. They are where institutional investors were a few years ago – relying heavily on ESG ratings and using the available data for aggregation or to get a general sense.

There are dozens of ratings out there, none of which seem to fully agree. Ratings may also be backward-looking with no real-time information flowing into them. Rather than relying on ratings, the best approach is to figure out what information makes most sense for your portfolio, find the raw data, and apply it in context to your own risk framework.

Ratings can be used by insurers as a first step – if the rating looks good, an insurer may decide to provide coverage without deep scrutiny. If the rating looks questionable or elevates certain risks, the insurer can conduct a deeper dive to see if there are mitigating factors.

This is where engagement with corporate issuers is incredibly important. Giving companies a direct line of conversation about what you expect and how you’re evaluating ESG risks can push them towards enhanced disclosure.

However, it requires a lot of resources from the insurer to adequately gauge ESG risk, and from the company to provide the information. Insurers also need to put processes and tools in place to ensure underwriters are not left alone with these decisions, because interpreting ESG data can be a huge task.

> “Insurers need to put processes and tools in place to ensure underwriters are not left alone with these decisions.”

2.3.4. ESG data providers

Beyond rating agencies, insurers can access third-party ESG risk data, scores and assessments from a growing range of specialist data providers.

These can be broadly split into three buckets:

- **Data generalists** for whom ESG solutions represent an important growth segment (e.g. MSCI, Bloomberg);
- **Risk and insurance data providers** who are expanding their offerings to insurers to include ESG data (e.g. RMS, Verisk Maplecroft); and
- **ESG data specialists** who serve multiple industries including insurance (e.g. Sustainalytics, RepRisk).

Many of these providers began providing ESG data in the investment space before developing capabilities specifically to serve the insurance industry.

PCAF told us it commissioned a study which found at least 60 data providers offering emissions data. Across such a broad marketplace, USPs and data granularity, quality and metrics vary significantly. This can make the choice of partner(s) overwhelming for insurers.

2.4. Data blind spots

Data capture is particularly challenging in the pockets outlined below.

2.4.1. Private sector

(Re)insurers told us capturing reliable ESG data on private companies is a key challenge, particularly when dealing with SMEs. While it is possible to capture publicly available data or purchase ESG data or ratings on most public companies in most developed markets, this information may only be available on a private company by asking directly – though this doesn’t always work.

Without reporting obligations or shareholder pressure to disclose ESG performance, private companies may not be motivated to disclose. Smaller companies may also have less resources to allocate towards collecting ESG data and see it as a burden.

Sector proxies eoncompassing the private sector play a key role in helping (re)insurers quantify ESG risks within their portfolios but are only a guide.

Coverage of the private sector is slowly improving, with many leading providers expanding their capabilities. However, there is a long way to go.

> “Even among data providers the understanding of ESG data needs to improve. ESG data is big business, and we must prevent the ‘pretend before you can really do’ attitude.”
>
> *– Patricia Kern, Poseidon Principles for Marine Insurance*

> “We work with external data providers and supplement that with internal risk assessment data and research.”
>
> *– Reinsurer*

> “The insurance industry needs to agree a succinct list of questions that are statistically relevant to ESG and readily available from SMEs which can be collected as part of the underwriting process.”
>
> *– Salman Siddiqui, Moody’s Analytics*

“On SME binders, the cost of asking ESG questions could be more than the premium.”

– Insurer

“There are quality issues in scopes 1, 2 and 3 emissions data. However, scope 3 is much more complex.”

– Broker

“We’re all at different levels, have different regulators and lines of business are so varied in where we are on the ESG journey.”

– Insurer

“One of my roles is get the group office to understand what we need in the UK. ESG is not currently built into their strategy.”

– Insurer

2.4.1.1. Swiss Re/Lloyd’s Lab project

In March 2022, Swiss Re joined the eighth cohort of the Lloyd’s Lab accelerator programme for insurance innovation, with a focus on improving private company ESG data.[20] Its project aims to develop a clickable prototype to collect and view private companies’ data, relevant to agreed ESG metrics, to help insurers decarbonise their portfolios.

2.4.2. Scope 3 emissions

(Re)insurers admitted they are struggling to quantify the scope 3 emissions within their underwriting portfolios (i.e. the emissions that exist within insureds’ often complex value chains). Many underlying companies are only just beginning to tackle this issue themselves.

For diversified organisations with large value chains, quantification is highly complex. Insurers have limited look-through into clients’ suppliers, particularly beyond tier 1.

The challenge becomes even more complicated when addressing less quantifiable ESG factors than GHG emissions, though it is possible for (re)insurers to ask whether clients stipulate certain behaviours of their suppliers.

Where data is unavailable, sector proxies again serve a purpose.

2.4.3. International and sector-based variations

Regulatory, stakeholder and corporate approaches to ESG vary significantly by jurisdiction. (Re)insurers told us that, broadly speaking, regulatory activity in the EU has made European clients far better at answering ESG questions than those in developing markets and the US. This poses data capture challenges for insurers with diverse global books of business.

Certain sectors are also more advanced in their ESG disclosures and may be more focused on specific metrics than others. High emitting sectors like oil & gas, for example, have been reporting GHG emissions for some time and do so as a matter of course.

Sustainability champions in global insurance groups may even find cultural roadblocks within their own organisations. Some UK-based insurers told us their leaders in the US are behind the curve on the ‘E’ aspect of ESG. One said the same of a head office in Europe. If counterparts in different jurisdictions are less motivated to ask ESG questions of clients, this can make it difficult to embed ESG data capture in the underwriting process.

20. Meet Cohort 8, Lloyd’s, 2022

2.4.5. Nature risks

Nature is rising fast up the sustainability agenda, however, quantifying nature risk is highly complex, comprising multiple factors which are often interlinked.

Companies in most sectors are only just starting to evaluate the impacts they have on the natural world, let alone quantifying, reporting and target-setting on those impacts.

A survey of more than 1,200 companies conducted by CDP and Oliver Wyman in 2021 found that while 33% of companies had a water withdrawal target in place and 23% had a forest best practice policy, only one in 20 had SBTs in place for climate, water and forests.[21]

2.4.5.1. Materiality challenges

Insurers face a significant challenge to quantify and map the materiality of nature risks (and their many interdependencies) within their underwriting portfolios.

A good starting point is to develop an understanding of the key impacts certain industries have on nature, which can be used to flag risks that warrant closer investigation.

However, as natural systems vary by location, even generalising by industry is not straightforward as the impact a factory in Germany has on the surrounding environment may differ from the same type of factory in Brazil, for example.

For these reasons, many insurers do not know where to start with nature risk and are prioritising GHG emissions and other more easily trackable ESG factors. Others are working closely with TNFD and will play a key role in developing a workable methodology for underwriters to use when assessing nature risks.

TNFD has also developed volutntary guidance to help financial institutions in their assessment of nature-related risks and opportunities, known as the LEAP Framework:

LOCATE
your interface with nature
Identify where assets, operations, sectors, and value chains interact with nature, and areas of highest importance.

EVALUATE
dependencies and impacts
Identify size and scale of dependencies and impacts for business activities at priority locations.

ASSESS
risks and opportunities
Identify risks and opportunities, positive and negative impacts; their materiality; existing approaches applied and additional actions to take.

PREPARE
to respond
Define risk management, strategy and resource allocation decisions to take; how to set targets and measure progress; what to disclose, where and how.

21. Now for Nature, CDP/Oliver Wyman, 2022

“Insurers seek meaningful data to evaluate nature-related risks.”

Gunes Ergun

Engagement Manager, Marsh Climate & Sustainability Strategy & Secondee at TNFD

Insurers are looking to better understand the risks associated with nature and biodiversity loss across their portfolio both in terms of physical risks and transition risks. In general, we don’t lack data. With a few exceptions, such as in the ocean realm, there is already data available out there which corporates and financial institutions (FIs) can tap into to assess their value chains and portfolios. Supply chains remain the main challenge when it comes to data and traceability.

The Data Catalyst Initiative that TNFD launched in 2022 is particularly helpful to address those shortcomings in the current nature-related data landscape. It helps to identify the pain points but also opportunities to improve and scale decision-useful data and analytics in collaboration with service and data providers, FIs and corporates across the globe.

However, the data needs to be translated into useful metrics to inform decision-making and targets, which requires an enhanced awareness and willingness to understand nature and act on nature loss.

The TNFD LEAP Approach is part of the TNFD framework, and is designed to allow both corporates and FIs to assess their nature-related dependencies, impacts, risks and opportunities while preparing them to set targets and to report. TNFD is proposing a clear approach to scoping and materiality assessment when it comes to risk management and disclosure.

The TNFD has also started to design additional sector guidance, including sector-specific considerations for scoping, risk assessment and metrics. Understanding sector-specific nature-related risks and assessment criteria would help insurers to understand better their portfolios and act accordingly.

Along with TNFD framework development, both enterprise and risk valuation will evolve as there are simultaneous interests and concerted efforts by several standard setting institutions in this space. During COP 15, the International Sustainability Standards Board (ISSB) announced it will build a connection between the climate standards and issues around nature and ISSB is particularly interested in the recent work of TNFD.

Insurers are looking for meaningful data to evaluate nature-related risks, and I believe TNFD will help build the bridge between corporates and FIs, and shed light on corporates’ nature-related risks and opportunities.

2.4.6. Treaty reinsurance & delegated authority business

Treaty reinsurers and managing agents in the delegated authority market find it near impossible to get sufficient look-through into the ESG characteristics of underlying risks as coverage is typically arranged proportionally on a portfolio basis.

The quality and granularity of bordereaux – the reports ceding companies provide to capacity providers outlining their underwriting positions – can vary significantly across the market, particularly in non-property lines. They don’t typically contain any ESG data.

It may be possible to augment this basic risk data with third-party ESG data and/or proprietary research, though this is a costly and laborious process. For certain types of business, using sector-based or risk-based proxies may be the only feasible way for capacity providers to assess or quantify the ESG risks in their portfolios.

Treaty reinsurers and managing agents can exert influence over the behaviours of ceding insurers and delegated authorities by requesting certain practices, such as building back better in the restoration process, for example. However, it is hard to verify implementation.

One treaty reinsurer told us they are asking more qualitative questions at the point of underwriting to establish what type of ESG risks underlying portfolios may contain but have no formal process in place for what to do with the information.

Smaller MGAs undoubtedly need the guidance of more sophisticated partners on how to capture and disclose ESG data. Capacity providers must steer as best they can – though they may meet resistance, particularly outside of Europe.

One capacity provider told us they sent a questionnaire to delegated authorities in the UK and US asking whether these firms understood ESG and none of the US firms responded.

“Creating a treaty decarbonisation strategy is the next frontier, and the first step is to work with clients to create transparency.”

– Reinsurer

“Delegated authorities are behind the curve on ESG but it’s difficult to take a one-size fits all approach. We have to clearly set out what we require as they find preparing ESG reports challenging.”

– Insurer

“We asked our MGAs if they understood ESG and how they assess their customers. US firms didn’t respond.”

– Insurer

“The journey for MGAs is just beginning”

Michael Keating

CEO, Managing General Agents’ Association

Gathering and using ESG data is still in its infancy among MGAs. However, both the company market and Lloyd’s are engaging with all stakeholders in how and what data should be gathered and how this may be used going forward. In some instances, and segments where this could prove challenging, both markets are encouraging a ‘transition’ phase.

Personally, I believe ESG will become integral to both risk appetite and pricing.

I’m encouraged around the proactivity of discussion and willingness to engage. MGAs are excellent at data but also receive many requests which, on the surface, do not add any value. This early engagement will assist in identifying what is critical, relevant, and therefore important.

All stakeholders will need to work collaboratively to deliver the right outcomes. MGAs should be discussing future requirements both with their capacity and broker partners, engaging with market events and embedding in their three-year strategic plans

Brokers, who know their customers best, should be embedding ESG data into both renewal and new business presentations. What that data looks like should evolve from the stakeholder discussions mentioned above.

The key, at this stage, is to recognise that the journey is just beginning. Requirements will change as we develop greater knowledge and understanding of what the data is telling us.

> “MGAs should be discussing future ESG data requirements both with their capacity and broker partners.”

3. Standardisation initiatives

In summary

- The insurance industry took some positive steps towards **standardising** ESG data in 2022.
- While there is no one-size-fits all solution to the challenges outlined in sections 1 and 2, incremental progress is being made in **targeted areas**.
- Standardisation of **GHG emission metrics** is a key focus as the industry sets sights on net-zero.
- **Lloyd’s** is developing a data strategy to enable its members to transition.
- Companies including Moody’s and WTW have launched well-received **commercial solutions** that bring some standardisation to insurance ESG data.
- **Sector-specific initiatives** like the Poseidon Principles for Marine Insurance could provide a template for other classes of business to follow.

3.1. NZIA/PCAF Insurance-Associated Emissions Standard

One of NZIA’s key objectives is to establish a consistent data and metrics framework.

Following a period of industry consultation, Version 1.0 of the NZIA’s Target Setting Protocol was launched in January 2023 to enable NZIA members to begin to independently set science-based, interim decarbonisation targets for their underwriting portfolios. An expanded Version 2.0 of the Protocol will be published by 31 December 2025.[22]

A key milestone was the launch at COP27 in November 2022 of the Global GHG Accounting and Reporting Standard for Insurance-Associated Emissions - a collaboration between the NZIA and the Partnership for Carbon Accounting Financials (PCAF).[23]

This is the first global standard to measure and disclose emissions attributable to insurance underwriting portfolios. The standard is open source and publicly available for anyone to adopt. PCAF member companies can also access technical assistance and a database of over three million emission factors (primarily related to building and motor emissions).

16 (re)insurers were involved in developing the standard, which:

- Defines attribution factors for commercial lines portfolios and personal motor portfolios;
- Provides a framework for (re)insurers to measure and disclose GHG emissions associated with their underwriting portfolios; and
- Provides guidance on emissions data, data quality, and reporting requirements and recommendations.

22. NZIA Target-Setting Protocol Version 1.0, NZIA, 2023
23. PCAF launches the Global GHG Accounting and Reporting Standard for Insurance-Associated Emissions, PCAF, 2022

> Simplicity and the use of readily available data was top of mind in the development process. I'm confident that this will support the rapid adoption by the industry. The Standard can be applied to more than 70% of the global property and casualty primary insurance market and the working group aims to extend its scope.
>
> *– Thierry Léger, Group CUO, Swiss Re*

> We are concerned there won't be as much consistency as we'd hope – at least not at the start – because there are options to not report on everything and to take different views on scope 3. I'm not sure it creates a level playing field.
>
> *– Insurer*

Some (re)insurers told us the Standard would bring some much-needed consistency to emissions quantification. However, one broker criticised the Standard for failing to consider clients' transition plans. Others were worried NZIA and PCAF were leaving leeway in measuring and reporting insureds' scope 3 emissions, particularly as there were some small but significant differences between the draft Protocol and Standard wordings.

This was addressed in version 1.0 of the Protocol, which aligns with the Standard's stance on scope 3. Rather than saying 'may', the Protocol now states: "NZIA members *shall* cover a re/insured's attributable Scope 1, Scope 2, and—where significant and where data allow—***should*** cover a re/insured's attributable Scope 3 emissions in their IAE reduction targets".

Activist group Insure Our Future claimed that in making insureds' Scope 3 emissions reporting "optional", this violates Race to Zero and UN High Level Expert Group on Net-Zero Emissions recommendations. However, the reality is (re)insurers are reliant on insureds quantifying and disclosing their scope 3 emissions, and in the current environment, they will have little option but to rely on reasonable and verifiable estimates in many cases.

PCAF sharpens focus on insurance data

PCAF has built a database of over three million emission factors, which are publicly available, for different sectors, real estate and motor vehicles which was designed primarily to help financial institutions to calculate emissions in their portfolios. All PCAF signatories have access to this database. PCAF also runs a database with emission factors for different building types in Europe.

"With some tweaking, this data could be valuable to property and motor insurers," said Marco Tormen, Europe & DACHLI Regional Lead, PCAF. "Ideally insurers can get information from clients, and public sources and associations, but if all else fails, the PCAF databases can help.

"We may have to make some changes as some of the data is probably too granular and some potentially valuable data points for underwriters may also be missing. But without a single point of access to emissions data, insurers will have to pay a lot of money to data providers, so let's try to make this data available to everyone.

"One central emissions database is our final goal, but it will not be easy to get there. We also plan to develop standardised question templates for underwriters, which may be included in future versions of the Global GHG Accounting and Reporting Standard for Insurance-Associated Emissions. There is already a first template with questions available in the launched Standard."

3.2. Lloyd's data standardisation efforts

Lloyd's was an early signatory of the NZIA, committing to guide the market towards net-zero underwriting by 2050. Improving and standardising data capture and, where possible, implementation in underwriting processes, will be key. This is a huge and complex task.

Lloyd's is a diverse market, spanning large syndicates with stated ambitions around ESG through to micro brokers and MGAs which address ESG only when mandated to do so. Lloyd's must address ESG data while balancing the needs of all members and stakeholders and is currently capturing information on members' broader ESG strategies, including how they capture data and engage with clients.

It has publicly shared an ambition to measure the emissions of the market and is considering what additional data may be needed from the clients to do this. However, it is expected that, given the visibility issues in delegated authority and treaty business (see section 2.4.6.), as well as the complexity of the market's distribution chains, sector proxies will play an important role. It is likely that these disclosures will be compulsory by 2024.

Lloyd's is also keen to standardise approaches among insurers operating in certain classes of business to ensure the market moves in alignment, as well as facilitating data aggregation and avoiding inefficiencies like the need to validate individual company methodologies.

We understand this may eventually include a centralised process which could give all market participants access to a shared single source of truth and minimise the administrative burden on insureds.

A nearer term goal is to develop standardised question sets. Progress is already underway, as evidenced by the Joint Natural Resources Committee Transition Questionnaire for offshore energy underwriters (see section 2.1.3.).

Lloyd's will not, however, suggest ESG risk scoring methodologies to its members as this could influence their underwriting decisions, raising antitrust issues.

> All PCAF focuses on is point emissions. Insurers also need to understand their clients' transition commitments, otherwise this is just an accounting exercise. That said, any proposal will be flawed and that shouldn't stop us supporting it.
>
> *– Broker*

> We hope to join the NZIA, but we've got to be comfortable with the NZIA's proposal on how to deal with scope 3 emissions before we commit.
>
> *- Reinsurer*

> “The market needs to talk consistently about ESG, even if companies take different internal views. Our long-term vision is to create a market standard across the value chain.”
>
> *– Salman Siddiqui, Moody’s Analytics*

> “Insurers want want ownership and accountability of the methodology they use. Our flexible approach gives them the framework to do so.”
>
> *– Paul McCarney, Moody’s Analytics*

> “We’ve never seen a topic evolve this fast.”
>
> *– Salman Siddiqui, Moody’s Analytics*

3.3. Moody’s/Chaucer ESG Balanced Scorecard

In 2022, Moody’s and Lloyd’s (re)insurer Chaucer collaborated to develop an ESG scoring and management solution – the ESG Balanced Scorecard – which enables (re)insurers to implement a consistent enterprise-wide approach to ESG risk assessment across their underwriting, investments and operations.[24]

It uses over 150 unique data points to assign scores for corporates across E, S and G, as well as an aggregated score, based on criteria and weightings determined by the insurer.

Portfolio analytics enable the insurer to view, rate and stress test their portfolio through various lenses (e.g. line of business, location, ESG risk factor, etc.) and to assess its alignment with its commitments and report to stakeholders.

Moody’s claimed the solution offers strong coverage of private companies and SMEs, leveraging “robust proxy modelling” where data is lacking. The scorecard will soon include a carbon intensity score for each company.

At the time of writing, several other insurers, including Canopius, were working with Moody’s to develop their own versions.

How the ESG Balanced Scorecard works

- The insurer determines its ESG scoring methodology (i.e. criteria & weightings).
- The insurer uploads its underwriting/investment portfolios and/or suppliers .
- The system finds and matches the underlying companies within Moody’s database.
- It delivers E, S and G scores plus an aggregate score for each company based on the insurer’s scoring methodology.
- Analytics layers enable granular analysis, target-tracking and reporting across the portfolios.
- The insurer determines what actions to take based on these insights.

24. Chaucer, in collaboration with Moody’s, embed their ESG Balanced Scorecard..., Chaucer Group, 2022

Operationalising ESG data

Salman Siddiqui
Senior Director, Insurance Practice Lead - Europe & Africa, Moody’s Analytics

Paul McCarney
Senior Director, Insurance Product Strategy, Moody’s Analytics

How will insurers use the ESG Balanced Scorecard?

The ESG Balanced Scorecard gives insurers a holistic view of ESG risks, supporting them in understanding and managing the impacts underlying companies have on people and planet as well as the financial impact on the company from ESG risk.

The Scorecard enables insurers to analyse, stress tests and understand key ESG drivers and exposures in their portfolios, and supports them in setting and meeting their commitments, be they net-zero targets or science-based targets. It then allows them to operationalise that data. Without bringing this data into portfolio management decision-making, ESG can’t go beyond being a box-ticking exercise. Additionally, workflow capabilities allow for seamless integration of ESG scores at the point of underwriting, allowing underwriters to engage more purposefully on sustainability with insureds.

It may be some time before insurers start using ESG data as a pricing mechanism, however, the Scorecard provides a valuable engagement point from which insurers can encourage disclosure and incentivise transition. We’re also seeing a shift in insurance from a product-centric to customer-centric approach. Accessing a rich vein of additional risk information should only help insurers understand and service clients better.

How do insurers’ approaches vary?

The market needs to talk consistently about ESG, even if companies take different internal views. Our long-term vision is to create a market standard just like there is a standard way of measuring natural catastrophe risk. As well as giving insurers consistency where it is needed, we also want to give them flexibility to develop their own methodologies. Our flexible approach gives them the framework to do so.

Some companies may want one scoring mechanism for all lines of business and investments while others may prefer a more nuanced approach as not all ESG criteria are relevant for every industry. Some may also want to take a different approach between underwriting and investments.

Where is there most room for improvement in ESG data?

The biggest challenge is accessing SME and private company data. We take a modelled approach to this universe and are working hard to bridge the gap between the large companies, which have a lot of disclosure, and small companies, for whom disclosure is very patchy.

The insurance industry needs to agree a succinct list of questions which are statistically relevant in influencing ESG scores as well as being readily available from SMEs. These can be collected from insureds as part of the renewal or underwriting process.

This is a fast-evolving topic and we’re sure our solution will look very different in two years’ time because so much will improve in ESG data. The speed of change over the last few months has been incredible. We’ve never seen a topic evolve this fast.

> Climate Transition Pathways (CTP) is there to help insurers differentiate risk quality or investment stability based on a client's willingness and ultimate track record on transitioning to a low carbon emitting future. It provides clients with a uniform way of monitoring this issue and an optimal way of addressing markets.
>
> *– Nick Dunlop, WTW*

3.4 Climate Transition Pathways

Launched in 2021 by WTW, Climate Transition Pathways is an accreditation framework which enables organisations in high carbon industries to demonstrate they are executing against a robust transition plan so they can continue to access insurance and risk capacity through the transition.[25]

Companies undergo accreditation by CDP Worldwide, which assesses the alignment of their transition plans to the goals of the Paris Agreement.

Clients must demonstrate their transition plans:

- Are aligned to science-based targets or sector-based decarbonisation approaches;
- Are credible and focus on emissions abatement (carbon offsets don't count);
- Include an assessment of technologies which can be used to determine a decarbonisation pathway, aligned to the EU Taxonomy;
- Are backed by operating metrics rather than a commitment or pledge; and
- Enable them to track performance against the plan.

This type of accreditation brings consistency to transition plan reporting, distils the process into a single submission for the client which can be shared with multiple capacity providers, and reduces the risk assessment workload for underwriters.

The initiative is broadly lauded, notwithstanding its limitation to WTW clients.

3.5. Sector-based initiatives

In a fragmented ESG data landscape, industry-specific metrics and reporting frameworks can help insurers develop consistent and industry-appropriate methods with which to capture and quantify client data.

The Science Based Targets initiative (SBTi) has published sector guidance for 14 industries with the aim of bringing consistency to the way companies in these sectors measure emissions and set transition targets.[26]

Industry associations are also compiling data that can be used to create sector proxies. For example, the International Air Travel Association (IATA) has committed to net-zero by 2050 and the IATA is compiling data and publishing regular updates on its 300+ members' emissions. It also developed a Recommended Practice Pre-Passenger CO2 Calculation Methodology to encourage and standardise quantification in the sector.

25. Introducing Climate Transition Pathways, CTP
26. Sector Guidance, SBT

3.5.1. The Poseidon Principles for Marine Insurance

In the marine cargo segment, The Poseidon Principles for Marine Insurance (the Principles) launched in December 2021, giving (re)insurers a global framework through which to quantitatively assess and disclose the climate alignment of their underwriting portfolios.[27]

Developed collaboratively by the Union of Marine Insurance (IUMI), IMO and Global Maritime Forum in the wake of the Poseidon Principles for financial institutions, the Principles create a consistent global carbon emissions baseline and align insurers with the Paris Agreement and the IMO's ambition to reduce GHG emissions from international shipping by at least 50% by 2050 compared to 2008. The Principles will also be SBTi-aligned.

At the time of writing, the Principles had nine insurer signatories. They have committed to annually measure the carbon intensity and assess the climate alignment of their hull and machinery portfolios using the Principles' robust industry-appropriate methodology, data collection and analysis practices and knowledge-sharing and transparency requirements.

The establishment of the Principles was helped significantly by the pre-existence of the IMO's own GHG emissions data collection framework (see section 2.2.3). This enables insurers to capture data that is standardised worldwide, easily comparable and based on calculations rather than estimations.

Over time, the Principles may evolve to include ESG factors beyond emissions.

Insurers would benefit from similar frameworks being developed in other industries. Collaboration with industry bodies will be key.

27. Ensuring the future of responsible marine insurance, Poseidon Principles for Marine Insurance

> Industry associations can play an important role in collecting emissions data and providing it to the financial sector.
>
> *– Marco Tormen, PCAF*

> This is an evolving framework that should expand to the 'S' part of ESG as shipping is addressing its social challenges.
>
> *– Patricia Kern, Poseidon Principles for Marine Insurance*

“The Poseidon Principles are an opportunity for marine”

Patrizia Kern
Chair of the Drafting Committee, Poseidon Principles for Marine Insurance

When developing the Poseidon Principles for Marine Insurance, we were able to build on the well-established principles the Global Maritime Forum had developed for banks. This created a sectorial consensus we can be proud of.

As financial services companies, we aim to align with other stakeholders to create the right incentives for shipping companies to transition to a lower carbon footprint and to improve the corresponding risk profile

The Poseidon Principles are an opportunity for marine insurance in the context of the EU Taxonomy, as we are the first [class of business] to have a jointly agreed measurement for GHG emissions in place. This is notable for an industry sometimes perceived as conservative.

This is an evolving framework that should expand to the ‘S’ part of ESG as shipping is addressing its various important social challenges.

We are in this position because of the IMO and are extremely thankful to them. Without the IMO’s reporting framework in place, creating the Poseidon Principles would have been a lot more challenging.

We are seeing huge interest among insurers, but still some reluctance. Insurance companies will have to report under the EU Sustainable Financial Taxonomy. We have a common, straightforward methodology for doing so, so we should use it.

“Without the IMO’s reporting framework in place, creating the Poseidon Principles would have been a lot more challenging.”

4. ESG data implementation

In summary

- Many insurers are capturing ESG data but are **unsure how to act** upon it.
- Insurers are still in the process of **embedding** ESG data assessment in the underwriting process, with some lines of business more advanced than others.
- With the exception of some isolated sustainability-focused insurance business models, ESG data is not yet having a direct influence on the provision of **capacity** or the **pricing** of risk (with the exception of the broad exclusion of high-emission risks such as new thermal coal mining projects, etc.)
- Several firms are actively exploring the **correlations** between ESG factors and underwriting **performance**. In 2022, Howden and Fidelis released findings demonstrating a direct correlation.
- Insurers are currently more focused on **understanding** ESG impacts at **portfolio level** rather than eliminating poorly performing individual risks.
- In **five years,** many of the insurers we spoke to expect ESG data to flow into underwriting **dashboards** and **influence decision-making** and **pricing** along with other risk factors.
- Insurers and brokers believe companies with strong ESG credentials will eventually be **rewarded** with favourable coverage.
- At present, the implementation of ESG in the underwriting process is highly **inconsistent** and **labour-intensive**.
- Insurers face a **cultural** and **educational** challenge to enable and motivate underwriters to conduct ESG risk assessments.
- Improved data quality and standardisation would enable more ESG data capture and assessment processes to be **digitalised** and **automated**.

Once an insurer has captured ESG data it must convert those insight into actions. Insurers agree that ESG data in isolation has little competitive value but what they do with that data is where they may eventually carve out a competitive advantage.

The insurers we spoke to were at varying stages of maturity in terms of developing strategies for how to use ESG data and embed ESG data into the underwriting process.

“Decisions are not made with discrete data — they are made when relevant data comes together.”

– Raphael Zindi, S&P Global

“ESG data isn’t necessarily a competitive advantage for insurers today but may be in three or four years.”

– Ben Howarth, Association of British Insurers

“The financial services sector recognises we need to do the right thing, but the commercial factors also must align.”

– Nick Dunlop, WTW

"I believe ESG will become integral to both risk appetite and pricing."

– Michael Keating, Managing General Agents' Association

"I can see ESG having a significant impact on pricing in localised lines of business by 2030."

– Insurer

"If insurers say they won't provide capital based on ESG data they will put themselves in a weakened position because I can't see the whole industry moving as one."

– Broker

"We want to give our underwriters the confidence to use ESG data in the market, but this is going to take a few years."

– Insurer

The main areas of focus are the extent to which ESG ratings may influence underwriting decisions and pricing and the development of methodologies to quantify the ESG performance of underwriting portfolios for internal assessment and reporting purposes.

Insurers need to establish a coherent ESG data strategy to ensure the data is used to support their broader corporate sustainability strategies. This includes putting governance and procedures in place to ensure consistency of approach across the organisation.

4.1. Influence on underwriting decisions

The insurance industry is yet to take a firm stance on how ESG data affects underwriting decisions, capacity, terms and pricing.

Notwithstanding broad exclusions, none of the insurers we spoke to had yet clearly defined a strategy linking ESG ratings to risk selection or pricing. Most gather ESG data primarily to enable them to better understand their own ESG exposures and/or to flag poor ESG risks for referral or closer investigation. They are building up this data with the view that it will play a more direct role in underwriting decisions at some point in the future.

The ESG risk assessment process is largely undertaken manually by underwriters. Several insurers told us underwriters found ESG data capture and assessment burdensome.

Insurers also told us they find it difficult to communicate their approach to ESG externally beyond headline exclusions. One explained it was difficult to articulate a nuanced and qualitative approach in a world in which stakeholders demand facts and figures.

Many simply haven't yet decided how ESG data should be used. In some cases, ESG data is presented to underwriters but there is no obligation for them to act on it.

However, many of the (re)insurers and brokers we spoke to agreed that ESG is likely to have a significant impact on pricing, terms and capacity within the next five years. They believe ESG data will eventually be seamlessly embedded in the underwriting decision process alongside other forms of risk data, contributing to an insured's overall risk rating.

Brokers and (re)insurers told us they believe companies with strong ESG scores and/or a positive impact on environment and/or society will receive more favourable terms going forward.

As with all underwriting trends, this will need to be driven by ESG-minded 'leaders', with 'followers' falling in line only when regulators or market pressures force their hand. At the time of writing, there was little immediate momentum pushing the market in this direction.

One insurer said ESG data and ratings would have to improve significantly from today's state before they could influence risk selection and pricing.

Another suggested the debate over pricing may be a red herring as various ESG risk factors – particularly around governance – are already considered as standard when assessing an insureds' risk management approach and overall risk rating.

4.1.1. Engagement trumps exclusion

Many insurers have, as part of their net-zero commitments, excluded underwriting new business in various high-emission sectors such as coal mining and oil & gas.

However, it is impossible for insurers to withdraw capacity completely and immediately from these sectors without severely damaging their own balance sheets. Many of the companies with the worst ESG ratings are, after all, many of the longest-standing and financially valuable insurance clients in the world.

Insurers also argued there is also a societal benefit of engaging with existing clients to improve their behaviours rather than washing their hands of the problem by cutting ties. Given the proliferation of opportunistic capacity providers in the market, this business would simply be picked up elsewhere by insurers with lower standards who may be less inclined to steer underlying companies towards transition, they said.

One insurer also highlighted the need to balance social and environmental considerations, noting that developing economies need to meet the energy and food needs of their populations even if at the expense of the climate.

Insurers are therefore opting for responsible stewardship over exclusion wherever possible.

Open and transparent conversation with insureds is a key starting point. As insurers renew most types of insurance contracts at least once per year, this arguably gives them more steering power than banks as they can push for continued progress. One insurer, for example, said it grades insureds' ESG credentials and set targets for improvement over two- to three-year periods.

"At the moment, we are benchmarking our portfolio and building a view. If a company has a bad ESG score it won't prevent us writing business."

– Insurer

"Head office don't want to put their head above the parapet or restrict business in the short term."

– Insurer

"We need to create the right incentives for companies to transition by establishing KPIs and eventually seeing carbon footprint as a key risk driver."

– Reinsurer

"Why shoot ourselves in the foot before we have to? Until the market changes, we'll continue to sell certain products."

– Insurer

“You may believe companies which behave in a certain way are going to be less risky, but can you prove it? When we have enough data to verify the hypothesis, we can take stronger actions on terms and conditions.”

– Reinsurer

“We realised we can use ESG data across various lines of business in our portfolio to improve our bottom line. The work we've done so far has helped build a case to invest more into understanding this.”

– Insurer

“Underwriters need to be able to explain to their clients how ESG data is being used in the underwriting process – but they can't currently do that.”

– Amy Barnes, Marsh

At the same time, the annual renewal process can make insurance companies short-sighted. As climate-related risks may not materialise as insurance losses for many years, it is all too easy to overlook them to secure another year's premium from a client.

4.1.2. Emerging sustainable insurance models

There are isolated examples of insurance business models which directly reward companies with strong ESG credentials.

For example, in 2021, Marsh launched a directors and officers liability (D&O) insurance initiative that enables US-based clients with superior ESG frameworks to be considered for preferred D&O policy terms and conditions from a selection of participating D&O carriers.

In January 2022, Beazley launched Syndicate 4321 to provide additional capacity across a variety of lines of business to companies that perform well against ESG metrics. Beazley assesses their credentials in collaboration with S&P, Reprisk and Sustainalytics.[28]

Several specialist insurers, including Parhelion, GCube and Kita, for example, serve a broader sustainability agenda by providing insurance solutions that support climate solutions and energy transition.

However, these approaches are exceptions to the rule as the vast majority of insurers do not yet directly link ESG credentials to underwriting decisions in most lines of business.

4.2 Linking ESG and underwriting performance

Several insurers we spoke to were in the process of conducting internal studies to establish the potential links between ESG factors and underwriting performance.

The materiality of ESG risk varies significantly by line of business. While social and governance factors, from financial risk to labour relations, touch on virtually every sector, environmental risks like groundwater pollution or GHG emissions are more material to certain sectors than others.

In some lines, there are obvious correlations with insurance losses, including, for example:

- Environmental liability from pollution events;
- Liability losses related to climate litigation;
- Liability claims linked to poor governance or public safety ; and
- Climate-change or extreme weather-related property losses.

28. Syndicate 4321 supporting clients to transition, Beazley, 2021

In many other cases, the links are far from obvious. However, there is a working hypothesis that if a company scores well in ESG this equates to good governance and risk management. This theory is supported by a study released in 2022 by Howden and Fidelis (see box).

One rating agency also told us the claims portfolios it observed tended to have worse ESG ratings, though it has not formalised its findings.

One insurer told us it has been conducting an internal study which found clear causal correlations between ESG risk and event-driven D&O litigation as well as correlations (but not causation) in P&C lines. It said lack of data made it hard to draw conclusions in specialty.

If (re)insurers can clearly demonstrate a link between ESG and underwriting performance, this will make it much easier to win buy-in from underwriters and brokers on ESG data. However, Fidelis was the only insurer we spoke with willing to share a definitive view.

Landmark study links ESG to loss ratios

A joint study publicised in November 2022 by broker Howden and specialty (re)insurer Fidelis found that higher ESG ratings lead to better underwriting performance.[29]

The study of loss ratios across 30,000 policies from Howden and Fidelis' datasets (with a premium value of around US$9bn) against third party ESG ratings found environmental ratings have the strongest correlation with loss ratios, according to the analysis.

The study highlighted variations by line of business and industry. Of the multiple lines of business studied, property insurance shows the strongest correlation between better ESG scores and better loss experience, the firms said.

29. Higher ESG ratings lead to improved underwriting performance, Howden Group, 2022

“Underwriters don't mind trying to capture additional data if they know it's going to be used for, but we've been caught in traps of recording a lot of data that isn't going to impact pricing or reporting in a clear way.”

– Insurer

“Like investment managers, we'll probably look at whether the portfolio average score is acceptable as opposed to every single risk. The data isn't good enough to reject risks, but we can steer the portfolio in the right direction.”

– Insurer

“It's difficult not only to get ESG data but to quantify which data is relevant to each line of business and which models to use.”

– Insurer

"Not everybody wants to measure aviation emissions. If you find your aviation portfolio has a bigger impact than you thought, what do you do with that information?"

– Insurer

"Insurers need to put processes and tools in place to ensure underwriters are not left alone with these decisions, because interpreting ESG data can be a huge task."

– Laura Wanlass, Aon

"The limitations of ESG data don't stop us from trying to implement ESG guidelines into the underwriting process. There's a lot you can do without perfect data."

– Insurer

4.3 Portfolio-level quantification

A key near-term goal for insurers is to quantify the ESG performance of their underwriting portfolios. For companies that have committed to net-zero, accurately measuring GHG emissions across their books of business – and modelling their trajectory – is a necessity.

Some insurers may also need to benchmark the trajectory of their portfolios against a specific global temperature rise target. While this is a complex task, even a ballpark trajectory based on a basic methodology and reasonable assumptions can be of some value. The NZIA and PCAF will play a key role in establishing an industry standard for these calculations.

Insurers are also keen to understand the broader positive and negative impacts of their portfolios to identify which lines of business, sectors and geographies are hotspots for ESG risk in most urgent need of attention.

One insurer suggested there is some trepidation over what they might find. Aviation, for example, is a sector that has gone under the radar in the ESG conversation and has largely avoided exclusions by insurers despite being a major emitter of GHGs. "If you find aviation has a bigger impact than you thought, what do you do with that information?" the insurer asked. Another countered it is better to know than to bury your head in the sand.

Most (re)insurers we spoke to agreed it is more feasible at this stage to focus on steering portfolios towards acceptable aggregate or average ESG scores rather than taking a hard stance on every individual risk. In other words, it remains acceptable to insure poorly scoring companies provided the negative impacts are offset elsewhere in the portfolio.

One major reinsurer told us it aims to "cut through the insurer" to discover the impact of every underlying underwriting transaction so it can guide more capital towards more sustainable areas of the global economy.

However, (re)insurers are all at different stages of developing their internal methodologies for quantifying ESG risks at portfolio level.

4.4. Embedding ESG data in underwriting

Within five years, the (re)insurers we spoke to all want ESG to be ingested automatically into underwriting dashboards along with other risk factors to generate an overall risk score.

This would require them to develop their own internal ESG rating methodologies as well as determining how this data would affect risk rating and underwriting decisions. It would also demand a significant improvement in the quality and consistency of ESG data captured.

A very small minority of sophisticated companies have made some progress in developing internal ESG rating models and are in the early stages of integrating ESG risk into underwriting decisions in targeted lines of business.

For many, working out how to capture better ESG data capture and understanding its materiality to the business are still the top priorities.

Most insurers are still trying to define how their underwriting teams can contribute to their corporate objectives around ESG, as well as how the corporate function can enable underwriting teams in making those assessments.

4.4.1. Manual data capture creating a burden

Insurers also need to approach ESG data more efficiently. At present, many are allocating significant human resources to manually capture and/or assess ESG risks when underwriters are already extremely busy and facing a growing compliance and reporting burden.

One insurer told us its underwriters were spending up to four hours per risk generating qualitative ESG scores. This may be justifiable on a big-ticket client but is hard to justify across an entire portfolio of business.

As ESG becomes more all-pervading and touches more lines of business, (re)insurers will need more quantitative ESG data to flow into the underwriting process to enable them to digitalise and automate more elements of the process. This calls for higher quality, standardised, consistent ESG data at the point of capture.

"Aggregating temperature alignment at a portfolio level is very challenging. There isn't currently enough data, and you can't take a proxy approach because temperature alignment is an intention."

– Rating agency

"It's taking some of our underwriters up to four hours per risk to gather ESG data, which is not sustainable."

– Insurer

"We need to train underwriters around properly assessing ESG risks as not everyone will come to the same judgement given the same information."

– Insurer

"The individuals receiving ESG information need to understand what they're asking for. We've seen underwriters who don't know what scopes 1, 2 and 3 mean."

– Broker

"The younger generation of underwriters are more open to ESG, but those who have been doing things a certain way for a while can be harder to convince."

– Insurer

"You have to create a culture where people are taking accountability and the data is there to help them."

– Insurer

4.4.2. Enabling and motivating underwriters

Training underwriters on all aspects of ESG, including how to assess ESG risks and why these risks are material to insurance, is essential to enable underwriters to apply a consistent approach and to buy into the additional work required to capture and assess ESG data.

One insurer suggested underwriters may face a conflict of interest if presented with a choice between impact or profit. They said black and white guidance was needed – possibly agreed at industry level – to take some of those tough decision out of underwriters' hands.

Another pointed out it was not the underwriter's capital nor reputational risk on the line when they make decisions related to ESG.

Clear guidance should be provided to help underwriters in their decision-making, though it is also important not to swamp them with too much information.

Building an overall awareness and culture around ESG is also key. This is often set from the top down. Two people told us they worked for companies led by executives whose passionate views on sustainability, climate change, human rights and other issues set the tone for underwriters and had attracted talent with similar values.

Culturally, it may be harder to embed ESG data collection in lines of business in which underwriters have not traditionally been expected to gather much external data, and in which pricing models have remained unchanged for decades.

Insurance sustainability leaders told us it was important to speak in a language underwriters understand – focusing for example on the billions of dollars in opportunities presented by the creation of a new sustainable economy – and to also ensure they are clear on the organisation's overall values and objectives around sustainability issues.

Some have conducted workshops with underwriting leaders to ensure consistency of messaging and implementation.

Insurers may also increasingly consider linking underwriter remuneration to ESG-related KPIs. Some leading (re)insurers have established ESG-related KPI schemes and several insurers we spoke to were in the process of exploring this.

4.4.3. Leveraging operational efficiencies

Some (re)insurers told us their underwriting teams assess ESG risks independently from one another and are at quite different levels of maturity depending on class of business. They may therefore benefit from centralising processes and leveraging economies of scale within their organisations where possible (such as shared question sets and datasets) to drive both efficiency and consistency of approach across departments.

In some cases, underwriting teams may be able to work more closely with counterparts in investment teams, which often have several years' more experience assessing corporate ESG risks on the asset side. One insurer, for example, has a system in place whereby companies flagged as 'transition leaders' by either its underwriting team or investment arm do not have to be assessed by the other team.

Centralised ESG functions, orchestrated by sustainability officers or teams, can help embed processes and help build a culture around ESG data. However, many insurers are yet to invest in dedicated sustainability resources.

"I believe environmental and social impact is important, but I can't give that as the only reason – I need to bring purpose and the financial impact of ESG together in a cohesive strategy."

– Insurer

"If you can't get your underwriters to buy into the biggest economic challenge the world faces – climate change – you may need to take a look at your culture."

Ben Howarth, Association of British Insurers

"One of the challenges for us is to make sure that we have consistency across underwriting lines and across the group."

– Insurer

Addressing ESG data challenges

Global headwinds

- Regulatory trend towards disclosure (e.g. EU Taxonomy)
- Emerging disclosure frameworks (e.g. TNFD)
- Emerging transition plan frameworks (e.g. UK Transiti Plan Task Force)
- Establishment of standardised Science-Based Targets
- Greenwashing & reputational risk in the spotlight
- Politicisation of 'ESG'
- Increasing stakeholder expectations

Fragmented data landscape

- Proliferation of ESG factors
- Proliferation of commercial ESG solutions
- Proliferation of ESG data/rating providers
- Opaque rating methodologies
- Contradictory ratings
- Unstructured data
- Inconsistent reporting & metrics
- Data blind spots (e.g. nature, private companies)
- Lack of detail/accountability on transition plans
- Threat of greenwashing

Operational challenges

- Inconsistent insurer question sets
- Conflicting ESG goals and motivations
- Brokers bound to protect client interests
- Uncertainty over how ESG data is being used in underwriting
- Client resistance to disclosing 'non-risk' information
- Resource burden on clients, brokers & underwriters
- Lack of transparency in treaty & delegated authority business
- ESG training and culture needed for front line employees
- Profit versus purpose
- Underwriting margins under pressure
- Relationship management

REINSURERS
INSURERS
BROKERS
INSUREDS

Mitigating actions

- Collaborative insurance initiatives (e.g. ClimateWise, NZIA)
- Insurance-associated data initiatives (e.g. PCAF-NZIA emission standard)
- Broker-led disclosure frameworks (e.g. Climate Transition Pathways)
- Sector-based emissions initiatives (e.g. Poseidon Principles)
- Improving third-party data coverage & ESG solutions (eg, Moody's ESG Balanced Scorecard)
- Standardised question sets (e.g. JNRC Transition Questionnaire)
- Studies linking ESG and underwriting performance (e.g. Howden-Fidelis)
- Growing number of net-zero commitments and underwriting exclusions

Future goals

- Insurers access better data – coverage, accuracy & consistency
- Development of centralised/shared ESG data/ratings resources
- Greater standardisation of ESG data in the underwriting process
- ESG data flows seamlessly into underwriting dashboards
- ESG influencing capacity, terms and/or pricing
- Technology enabling greater digitalisation & automation
- Increased industry collaboration

> "There is a lot of confusion, distrust and suspicion about what information is needed, how it's going to be used and how will it affect clients' ability to get business placed."
>
> *– Broker*

> "It's not right to ask for data and not tell the client what you're going to do with it."
>
> *– Nick Dunlop, WTW*

> "One insured thought that if they majored on the 'S' & the 'G' they might get let off the hook on the 'E', but that just isn't true."
>
> *– Broker*

5. The need for collaboration

In summary

- (Re)insurers and brokers crave a **common language** for ESG.
- Brokers accept insurers will take slightly different approaches to ESG but want the industry to agree on key **metrics** and **question sets**.
- Brokers also want insurers to **reveal** how client ESG data affects **underwriting decisions**.
- Insurers may not be ready to **articulate** their internal processes as they are still works in progress.
- Insurers are **surprised** how little ESG data **reinsurers** are currently asking them to **disclose**.
- Reinsurer information requests are largely **qualitative** but are becoming more detailed.
- Differing opinions on who should be **leading** on ESG data has led to **inertia**.
- Insurers, brokers and reinsurers all agree **collaboration** is needed with each other and among competitors to improve the quality and consistency of ESG data.

All industry stakeholders we spoke to agreed collaboration is essential across the insurance marketplace to overcome some of the key challenges and improve the quality and consistency of ESG data in the insurance process.

However, there is some uncertainty over who is ultimately responsible for driving change. A lack of communication between counterparties has also led to some distrust.

At the start of 2022, the market was in a standoff. However, several initiatives have since been launched which may at least partially address some of these problems (see section 3).

5.1. The insurer-broker relationship

5.1.1. Broker frustrations

Brokers' core objective is to place their clients' risks as quickly and efficiently as possible, at the best price and coverage terms. ESG data requests slow this process and a lack of transparency from insurers over the implications of the answers causes some unease.

Brokers (and their clients) are also increasingly frustrated by the unnecessary work ESG questionnaires can create if each insurer takes a slightly different approach (see section 2.1.5).

Brokers accept there will be some differences in the type of ESG data insurers ask of clients. However, they believe the many commonalities between information requests justifies the establishment of some core metrics and questions to be used across the industry.

The brokers we spoke to also wanted more transparency from insurers over how ESG data is used and whether it directly influences insurance coverage, pricing or terms. Where there are no policy implications, this becomes a tricky grey area to navigate as brokers and clients may question the relevancy of the information being requested.

Brokers explained how certain clients are fearful of disclosing ESG data because they don't know whether it will hinder their ability to obtain affordable coverage. In some cases, the broker's own commitments to net-zero or ESG targets may also sit at odds with their duty to place business on behalf of companies in poorly performing sectors.

Brokers also noted there can be dissonance between the messaging from insurers at corporate level and the attitudes of individual underwriters on the ground.

Insurers report that some brokers and clients are proactively reaching out to understand their approach to ESG and what data to provide.

5.1.2. Insurer responses

The insurers we spoke to accepted the status quo was unacceptable and unsustainable. They value their client and broker relationships and are concerned about placing a burden on them.

> "As a client, the worst thing you can do for your ESG score is to not disclose."
>
> *– Ben Howarth, Association of British Insurers*

> "If you don't have a human rights policy, you get the same score as someone who murders children – zero."
>
> *– Insurer*

> "It's difficult to articulate internal stuff we don't want to share or is too qualitative to manage."
>
> *– Insurer*

> "Beneath the big three brokers, the approach of brokers to ESG data is completely different. Most are not sensitised to the topic. They need to evolve their processes and start asking the right questions."
>
> *– Insurer*

“ The more transparency we can enable as an intermediary, the better we can enable the climate transition, develop new solutions and make society more resilient. ”

– Broker

“ In an ideal world, clients, brokers and insurers should be leading together. However, insurers are in a privileged because that's where the buck stops. ”

– Brokers

“ Many clients in carbon intensive industries are fearful of the disclosures they're being asked to make because they think it could result in an automatic prohibition. ”

Amy Barnes, Marsh

They also agree that ESG risk data alone is not competitively sensitive. That value is created in how the data is used. They are therefore open to some collaboration with competitors.

However, we found some reluctance to sharing class-specific question sets, particularly when the work put into adapting these for specific industries could constitute intellectual property.

Insurers are also wary of giving too much away to clients about their internal processes. The primary issue is that most are still working out for themselves exactly how ESG data will influence underwriting decisions going forward.

Another problem is that if they tell clients too much about their ESG rating methodologies, this could equip the client with potential loopholes to exploit in their answers.

At the same time, insurers suggested that if clients fail to disclose, this is likely to reflect negatively on them as an ESG risk.

5.1.3. Meeting in the middle

Proactivity and compromise are necessary from both insurers and brokers to bridge the gap.

Ultimately, insurers are the companies requesting ESG information. They should know what they want and therefore lead the conversation. They should also be able to explain at least in broad terms why they are asking for certain information.

At the same time, brokers have a broad market view which means they are well positioned to guide the market towards standardised question sets and metrics (which the bigger players are attempting to varying degrees).

It is, after all, in the broker's interests to steer the industry towards an approach that is workable for clients while also 'controlling the narrative' on their behalf.

Where common ESG metrics such as GHG emissions are concerned, insurers could be more proactively collaborating with competitors to develop core class-specific question sets.

Ultimately, all parties we spoke to agreed brokers and insurers need to work together to find solutions.

“Insurers can't currently explain how ESG data is used”

Amy Barnes

Head of Sustainability & Climate Change Strategy, Marsh

I think it's reasonable for insurers to understand if their clients are doing anything harmful. We also believe there are parts of the ESG agenda which are aligned with risk, so I feel very comfortable with insurers having access to that information.

However, it's not my job as a broker to embolden insurers to make the underwriting process more complex for clients. What information can underwriters legitimately ask for if it is not informing underwriting risk?

Are questions driven by underwriting or Know Your Client? Why should we answer questions about strategy that we normally wouldn't have to answer?

Many clients in carbon intensive industries are fearful of the disclosures they're being asked to make because they think it could result in an automatic prohibition. If there is no clarity on the consequences for the underwriting decision, what is the motivation to disclose?

Underwriters need to be able to explain to their clients how ESG data is being used in the underwriting process – but they can't currently do that.

“ If there is no clarity on the consequences for the underwriting decision, what is the motivation to disclose? ”

“I've been surprised there hasn't been more demand for detailed information from our reinsurers, though as stakeholder expectations evolve and everyone looks to their supply chains, I expect it to build.”

– Insurer

“If we can report to reinsurers, third-party capital providers and investors that we've got ESG right, it could be a competitive advantage for us.”

– Insurer

“In many ways, reinsurers call the shots – they are putting their balance sheet at risk and are at liberty to ask for whatever data they want.”

– Insurer

5.2 The insurer-reinsurer relationship

As capacity providers, reinsurers are uniquely positioned to steer the insurance industry towards a more stringent approach to ESG, in turn accelerating the role of insurers in steering corporate behaviours. Several major reinsurers have stated they will exclude the reinsurance of certain high-emitting sectors such as coal mining and oil & gas.

However, reinsurers are in general playing a passive role when it comes to ESG data. Several insurers told us they are surprised how little ESG data reinsurers are asking of them, though some reinsurers are beginning to request more detailed information. If information is requested by reinsurers, it is most likely to be high-level fact-finding designed to understand where the insurer is on the ESG maturity curve and its transition plans.

Answers provided by the insurer are unlikely to have any bearing on capacity, pricing or terms at this stage (except where there may be a breach of ESG-related exclusions laid out by the reinsurer).

One reinsurer admitted there is little structure to its own approach at this stage, and that insurers and reinsurers are “feeling each other out” to get a sense of their transition plans. Another said it was finding it difficult to establish a methodology for assessing insurers.

As outlined in section 2.4,6 it is particularly challenging for treaty reinsurers to get granular look-through into underlying insurance portfolios. One treaty reinsurer told us that if underlying insureds have signed up to reporting frameworks like TFCD, this can flow through bordereaux reports and can then be verified by the reinsurer.

The same reinsurer has also implemented ‘soft’ internal procedures such as mandatory referrals to the CUO, with input from the sustainability officer, on all new energy business.

Going forward, insurers said they expect reinsurers to ask for more specific information around GHG emissions and other key ESG metrics. One suggested proactively providing ESG data to reinsurers could even become a competitive advantage in the future as it would mark the insurer out as an attractive partner to work with.

As with the broker-insurer relationship, greater collaboration and engagement is needed between insurers, reinsurance brokers and reinsurers to improve transparency and drive standardisation and consistency of disclosure in the reinsurance process.

RenRe's Cathal Carr on being more proactive

Cathal Carr, SVP, Chief Underwriting Officer - Europe, for RenaissanceRe, told us he wants to see improved ESG data flow within the reinsurance value chain - but this calls for proactivity.

“Most reinsurers want to enable the climate transition, but they are not getting much ESG data from insurance companies, so their mentality is to sit back, wait for insurers to sort this issue out and send them the data, then they'll work out what to do with it,” he said.

“My role is to ensure we are more proactive than that in terms of how we measure risk and impact within the reinsurance process and how we drive change right through the supply chain.”

“We're starting to ask more questions but there is no consistency and no formal process in place for what underwriters do with the answers.”

– Reinsurer

“It's challenging to come up with an approach to assessing insurance portfolios.”

– Reinsurer

“We are presented with data designed to get us on the risk, not necessarily to inform us the most. The insurer and its broker want to get the deal done.”

– Reinsurer

“We want to hold ourselves to the same standard”

Andrew Smith
Chief Risk & Sustainability Officer, Conduit Re

Conduit Re is a primarily a treaty reinsurer. For reinsurers in the subscriptions market, it is difficult to guide underlying insurers other than explaining our appetite, approach and philosophy, and collaborating with industry ESG working groups.

From an ESG perspective, we’re starting to ask more questions at the time of underwriting to get a general flavour of insurers’ transition plans. We might also ask an insurer to identify the 10 biggest insureds in their portfolio so we can do some deeper ESG analysis in the same way as we do through a pricing and reserving lens.

When we think about what we might ask people, we want to make sure we would be able to hold ourselves to that same standard. There is a natural tendency in the insurance industry to focus on what we won’t we cover – not just in ESG but any form of risk – and the danger is we create sets of questions that will push people onto a path of exclusions, which we don’t think is helpful for maintaining and growing the insurable landscape sustainably.

The information we need varies by line of business, but we’d like to ask a standard set of questions around ESG. There is a huge role for brokers to play as, over time, they will understand what questions we ask and come back with and can begin to pre-empt them. We are also producing some information to share with partners which explains what we write and why we write it, and to show cedants we are on the same page.

As transparency improves, we expect more rigid underwriting rules to come into place around ESG in the years ahead, with wordings on specific coverage moving incrementally.

> “The danger is we create sets of questions that will push people onto a path of exclusions, which we don’t think is helpful.”

Who should lead on ESG data?

“Insurers are in a privileged position because that’s where the buck stops.” – Broker

“It’s not the broker’s role to determine how insurers weight ESG.” – Broker

“Broker competition to offer ESG solutions is a barrier to collaboration and universality.” – Guy Dormer, LMA

“If insurers don’t provide us with ESG data, we simply don’t have the line of sight to steer the insurance industry in the direction it needs to go.” – Reinsurer

“It’s hard for us to articulate our internal approach publicly” – Insurer

“Our reinsurers haven’t asked for much input other than a summary of our ESG approach, which is surprising as many are market leaders.” – Insurer

Ultimately, everyone needs to take a more proactive role…

“You don’t have to be alone with ESG data. There are a lot of resources that smaller players can tap into. Join forces and work with others.” – Reinsurer

“Ideally, clients, brokers and insurers should be leading together.” – Insurer

“The reinsurance industry is very open to collaboration and our successes have often been achieved as a market. Every company in the industry needs to play its part and work out where it can make a meaningful contribution in ESG.” – Andrew Smith, Conduit Re

“In PCAF, competitors are willing to share data sources, the types of data they found, and stories of how they overcame difficulties in their calculations. No-one is alone.” – Marco Tormen, PCAF

6. NEXT STEPS FOR INSURERS

Every insurer and reinsurer has its own unique objectives around ESG data and is at its own stage on the maturity curve. Regardless of motivation or preparedness, all (re)insurers must establish an ESG data strategy because ESG data will undoubtedly play an increasingly important role in the underwriting process in the years to come – from increased reporting requirements to the potential for the market to start rewarding companies with superior ESG credentials.

For companies just getting started with ESG data, implementing a coherent strategy may feel daunting. For more companies with a more mature approach, the coming years will all be about optimising the quality of ESG data captured and embedding it within the underwriting process. Below we outline the three key steps to put (re)insurers on the path to ESG data maturity.

1. Define the ESG data strategy and operating model

(Re)insurers must first set a clear ambition for ESG data for underwriting with senior leadership buy-in – the 'North Star' which aligns with and supports the objectives of the company's broader ESG/sustainability vision. This includes identifying which ESG factors are most material to the organisation and its ESG/sustainability goals.

Those objectives could include, for example:

- Meeting net-zero or Paris alignment commitments;
- Protecting the company against ESG-related financial or reputational risks;
- Improving the company's social and environmental impact across various ESG factors (e.g. nature, human rights, closing the protection gap, etc.);
- Measuring the impact of ESG factors on underwriting performance and improving profitability;
- Meeting regulatory or stakeholder reporting requirements; and/or
- Becoming a market-leader in sustainable insurance solutions.

The insurer must then define how it intends to act upon the data. Is the data designed to build a better understanding or will it directly influence underwriting decisions?

Both insurers and (re)insurers also need to define the scope of their ESG data ambition: do insurers want to cover all lines of business, or only those with a high environmental impact, for example? Do reinsurers have an ambition to include treaty or focus solely on facultative? This should include being clear on the final output – will there be specific metrics on a dashboard driving underwriting decisions, for example? This ambition will help define the data requirements.

(Re)insurers must also consider their operating models. Key questions include who will be responsible for the ESG data 'value chain' – from sourcing to testing and integrating into underwriting processes. Leaving responsibility with underwriters risks inaction, whereas pushing centrally risks a lack of impact at the front line.

ESG data strategy drivers

DEFENSIVE
"We have to"

- Meeting regulatory reporting requirements
- Satisfying stakeholder expectations
- Mitigating reputational/ financial risks
- Meeting stated commitments

EXPLORATORY
"We want to understand"

- Measuring the impact of portfolios
- Measuring the impact of ESG on profitability

PROACTIVE
"We are striving to improve"

- Improving the company's social/ environmental impact
- Becoming a market-leader in sustainable solutions
- Leading the transition to a sustainable economy
- Providing ESG data service and solutions

2. Source relevant ESG data

(Re)insurers must next identify which specific ESG data allows them to execute on their strategy and achieve the outcomes aligned with their ambition. A company with a net-zero ambition, for example, will require more comprehensive GHG data than a company focused on adhering to the minimum regulatory requirements.

Once the outputs have been defined, the (re)insurer can work backwards to define what underlying ESG data needs to be captured on insureds (eg, scope 1, 2 and 3 emissions and transition plans).

Some of this data will need to be acquired directly from insureds, demanding the development of core questions to extract the relevant information.

Much of the data may be required from third parties. When choosing a data partner(s), in addition to considering costs, a (re)insurer should define the principles of what represents good ESG data, and:

- Test the provider's coverage of against the profile of the underwriting book;
- Conduct manual spot tests for reliability and consistency;
- Seek transparency of underlying data and the methodology driving ESG scores;
- Ensure the information provides the necessary metrics to meet its goals; and
- Continually re-assess and iterate given the changing nature of the data environment.

ESG data for underwriting should not be seen entirely in isolation from the broader ESG strategy (including investments). It will be important that the data abides by the (re)insurer's data standards, governance and/or other requirements.

“Have a very clear view of what you want the world and economy to look like in 2040 and what your role is in getting there.”

– Ben Howarth, Association of British Insurers

“Indecision happens when everybody is afraid of doing the wrong thing. We can't let perfection be the enemy of good.”

– Insurer

“ESG and sustainability can feel like trying to boil the ocean, but you have to start somewhere.”

– Reinsurer

3. Execute and embed

(Re)insurers must embed their ESG data strategy into their underwriting function. As ever, this is a mix of technical implementation and cultural transformation, requiring detailed operating model decisions and the appropriate governance overlay.

The technical requirements may include defining and embedding consistent processes using ESG data to create outputs. These will require, for example, methodological decisions on data gaps, assumptions on transition plans and target setting approaches.

(Re)insurers should work with trusted advisors to embed ESG data into underwriting processes in alignment with their broader ESG strategy, harnessing economies of scale and driving consistency across the organisation by developing centralised ESG resources, processes, question sets and shared datasets.

In addition, it is essential to build a culture of ESG which ensures underwriters are aligned with the company's vision and can articulate its approach when engaging with clients. Accountability for execution must be allocated to key personnel with clearly defined KPIs.

Insurers may also want to explore the role technology could play now or in the future to digitalise and automate certain ESG data processes to drive efficiency.

Insurers should also collaborate with competitors, partners and stakeholders to develop capabilities, drive best practices and accelerate standardisation. This could include aligning with collaborative industry initiatives (e.g. NZIA, ClimateWise, etc.) where appropriate.

Whilst the optimal approach may not be possible for all players immediately, setting out a clear ambition, and committing to taking action – even if only in targeted areas – is a must. The direction of travel is clear and (re)insurers will have the ability to deliver more thoughtful and impactful ESG strategies with the right data approach.

The insurance industry is moving into an era of greater sustainability, and all insurers will benefit from understanding their relationship with ESG and the role ESG data will play in future business models sooner rather than later.

> "Setting out a clear ambition and taking action, even if only in targeted areas, is a must."

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BETTER INSURANCE NETWORK

About
Better Insurance Network

Formed in 2021, Better Insurance Network is a growing community of insurance practitioners committed to driving best practices in sustainability through information-sharing and collaboration.

We partner with market-leading insurers, brokers and service providers to bring solutions and ideas to targeted groups of practitioners through events, research, networking and educational content.

Better Insurance Network produces the annual Sustainable Insurance Summit – a global virtual event which is the first insurance conference dedicated entirely to implementing sustainability in insurance.

Our membership includes insurance sustainability specialists, underwriters, brokers, senior leadership, operations, claims and HR professionals.

We believe the insurance industry is uniquely positioned to guide society towards a better future, and our mission is to help build a culture of sustainability and accelerate change.

Working together, we can help turn talk into action — not just among insurers but also the wider community of insureds, investees and communities our industry serves.

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Oxbow Partners

About
Oxbow Partners

Oxbow Partners is a specialist management consultancy exclusively serving the insurance industry. Our clients include leadership teams at the world's leading insurers, reinsurers, brokers and private equity firms.

Our consulting engagements span growth, operations, technology and M&A.

We have also built cross-industry expertise in ESG across the insurance sector, with an in-depth understanding of the ESG strategy of (re)insurers across the globe. We are uniquely placed to use this expertise in our engagement with (re)insurers on their approach to ESG.

Senior executives choose Oxbow Partners when they want a fresh perspective from a high-calibre team of industry specialists that thinks deeply about each client's unique situation and has a track record of delivering insight and impact.

We have applied for B Corp certification and expect to receive this in 2023. B Corp is an accredidation for companies that balance purpose and profit. B Corps are legally required to consider the impact of their decisions on their workers, customers, suppliers, community and the environment.

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