Society of Actuaries in Ireland

Consultation on Guidance for (Re)insurance Undertakings on Climate Change Risk (CP151)

Response to Central Bank of Ireland

October 2022

Preface

The Society of Actuaries in Ireland ("Society") is the professional body representing the actuarial profession in Ireland, and as such the Society and its members have a deep understanding of the Irish insurance industry.

The Society welcomes the opportunity to submit this response to the Public Consultation on the Guidance for (Re)Insurance Undertakings on Climate Change Risk. The response has been prepared by a cross section of members of the Society and does not purport to reflect the views of the insurance industry.

This document includes a response to the specific questions raised within the Consultation Paper. The text below also sets out the Society's views on this topic more generally.

General Comments

The Society recognises that the world's climate is changing at an unprecedented rate and that greenhouse gas ('GHG') emissions from human activity are the main cause. Climate change is already having major effects on the environment, the economy and society, and these effects are increasing over time. The Society supports the Central Bank's strategy to "strengthen the resilience of the financial system to climate-related risks".

Within the Society's membership, there remains a wide range in level of knowledge of climate pathways, applicable stresses and resources available to support the assessment of the impact of climate change. There is a growing body of literature available to actuaries, including the Society's own public statement on Climate Change matters and the series of "Climate Issues" papers produced by the International Actuarial Association. Against that, many members have to-date not even heard of NGFS. The Guidance seems to assume a level of knowledge of the existing climate change literature that can seem quite high to those with no prior knowledge. The Society believes that it would be particularly useful to smaller (re)insurers to provide additional signposting of areas that are considered assumed knowledge and specify resources deemed to be reliable, such as IPCC or NGFS publications.

Whilst recognising that there are a range of business models in operation in the Irish market and welcoming some of the flexibility provided by the guidance to allow for this range of business models, it is the Society's view that some more specific guidance would help drive more action in this area. In the view of some members, examples of some appropriate baseline climate scenarios - say along current projections published by the IPCC or NGFS - would remove some of the subjectivity for firms that do not have in-house climate experts and enable them to focus more on the materiality assessment.

In addition, the Society believes that some minimum standards, on a "Comply or Explain" type basis will assist smaller firms in getting started on their assessments.

The Society notes that the Guidance sets out one approach that can be taken; (re)insurers may use other approaches to those set out in the Guidance, providing that they produce similar outcomes. However, the Guidance is silent on *where* the outputs from this or alternative approaches should be documented and reported. In the absence of more specific emphasis on this point, financial professionals may more naturally lean on a ORSA / scenario modelling approach rather than a more narrative discussion on overall strategy and business model.

It is noted that the Central Bank's intention is not to introduce any new requirements on (re)insurers in relation to climate change risk. Rather, the Central Bank is seeking to clarify its expectations on compliance with the existing Solvency II prudential requirements relevant to climate change risk. We note these requirements have been evolving of late and it may be useful to some readers to include a summary of the existing requirements. We welcome the guidance in paragraph 7 that (re)insurers may use simplified or qualitative methods initially as part of an iterative approach that improves over time.

With reference to (re)insurers influencing the activities of those they underwrite, it would be useful for the CBI to give an example of acceptable (and unacceptable) expressions of influence.

Public Consultation Questions

Question 1: Are there any elements of the materiality assessment, or scenario analysis that stakeholders would like further clarity on and if so please specify which elements?

In carrying out a materiality assessment the Guidance identifies the (re)insurer's view of the future from a climate change perspective (i.e. baseline scenario) as a key component. Paragraph 38 goes on to note that (re)insurers may develop their own climate change baseline scenario or use publicly available scenarios.

The choice of baseline scenario generated significant discussion with different views held across members of the Society. A key barrier to getting firms engaged with climate risk is the "Where do I start?" question as noted in section 1.6 of the Consultation itself. Generally speaking, members from firms with lower PRISM ratings tended to have less experience in this area and to favour more prescriptive guidance in the form of a non-mandatory default baseline scenario. Practitioners with more knowledge of the existing literature tended to be more comfortable with the guidance as proposed and not to favour the inclusion of a default baseline scenario.

In particular, it was felt that the assessment of what is an appropriate baseline scenario requires either an in-depth knowledge of climate risk or reliance on a scenario defined by a third party such as the IPCC or NGFS. If less experienced firms are likely to ultimately use an IPCC or NGFS scenario, then perhaps suggesting a non-mandatory baseline scenario to start with would remove some ambiguity and assist firms in getting started. This would also potentially allow (re)insurers to focus on assessing the double materiality impacts of climate risk rather than getting overly immersed in climate science.

It is re-iterated that the Society members had different views on this point and perhaps an example of some suitable publicly available scenarios would help clarify the requirement here.

Similarly, again with less experienced practitioners in mind, it would be helpful for the Guidance to provide further clarity on the choice of stressed scenarios. For example, there could be a requirement for a minimum number of stressed scenarios (as EIOPA has done) or the Guidance could specify specific stressed scenarios. If stressed scenarios are specified, the onus should be placed on (re)insurers to ensure that they appropriately consider the climate related risks. Again, this would allow (re)insurers to focus on the impacts of a given scenario rather than trying to assess the likelihood of different climate scenarios which would be outside the expertise of many companies.

We also have some more specific points of feedback on the materiality assessment / scenario analysis:

- In relation to the materiality assessment, it is not clear from the Guidance if the materiality assessment is expected to be documented in the ORSA report or elsewhere? Additional signposting would be useful for (re)insurers who have not started their climate assessments to date.
- In Paragraph 45, the Guidelines outline that the feasibility of assumptions underlying management actions should be assessed and gives the example of 'societal acceptance of greater levels of uninsurable risk'. Further detail on the CBI's expectations in this regard would be helpful.
- In Paragraph 54 the phrasing 'may wish to consider' suggests a degree of optionality in assessing scenarios other than the baseline for those firms who do not have a material exposure to climate change risk; however, this optionality is not reflected in the infographic. We understand the intention of Paragraph 54 is to ensure that firms consider / understand their exposure to climate change across all reasonable scenarios so this optionality could be removed, and the text would then align with the infographic.

Question 2: Are there any other elements of the Guidance, or terms used, that stakeholders would like further clarity on, including the proposed infographic?

The Society notes a potential risk in a low exposure measurement due to the choice of a low climate risk baseline scenario.

Paragraph 61 asks (re)insurers to consider climate change risks over the longer term and reflect these in the overall strategy and business model. SAI members hold different views on this aspect of CP 151 with some viewing the point as requesting the entity captures its longer term thinking throughout its overall strategy and others of the opinion that the longer-term impacts and ensuing company actions may be too speculative to include in business strategy.

Paragraph 66 cites the CBI's expectation around the establishment of appropriate limits, thresholds and KRI's. Further clarity and examples around expected and appropriate KRI's would be helpful.

Paragraphs 80 and 81 speak to the possible risk of increasing numbers of uninsurable risks over the medium-to-long-term. Where a company sees this as a possible scenario for their business, the Guidance could include clarity around the CBI expectations on public disclosure of this kind of detail.

Paragraph 82 states that "insurers are also encouraged to consider how they may influence the activities of those they underwrite". The Society notes that current guidance from various bodies is relatively detailed on the treatment of investments in this area, however other (re)insurance activities are less clear. Further guidance, references or examples would be useful.

Box 7 states an expectation that (re)insurers ensure appropriate validation and review of the results of the models they use, particularly external models, such as Natural Catastrophe (NatCat) models. Validation can be relatively onerous for aspects of Solvency II. The CBI may wish to consider if this is the intention and/ or if different wording may better capture the intention.

The infographic gives a good flowchart of CBI's expectations. Further clarity would be useful with references to where the CBI expect each step to be documented.

3. Are there any items not mentioned in the Guidance that stakeholders think should be included, and if so please specify?

Similar to comments above, the Society believes it would be useful for their members if the guidance included recommendations on where (re)insurers might be expected to document their considerations.

This is a new and evolving risk type in an area where most (re)insurers do not currently have in-house expertise. Whilst the guidance does not introduce new "requirements", to comply with the guidance will require additional work and output from the existing teams.

In paragraph 12, "short term" is defined as 5-10 years. We suggest this should be 0-10 to reflect emerging experience and its classification as key risk in its own right (paragraph 8).

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