ARTICLE 5

The Crucial Role of Insurance in Facilitating a Just Transition

Insurers can help provide the social protection that communities need to participate in a just transition.

KEY TAKEAWAYS

- The transition to net zero will require financial safety nets to cushion the change.
- Insurance industry support for companies that prioritize a just transition can positively impact the economy and help bridge the skills gap.
- Affordable insurance is needed to support investments in emerging technologies.

Social protection for communities in flux: A role for insurance

As jobs in traditional industries make way for new clean-energy employment opportunities, the period of adjustment will be substantial. Financial safety nets are essential to support the transition of workers from traditional fossil fuel industries into new jobs in renewables and other clean-energy industries.

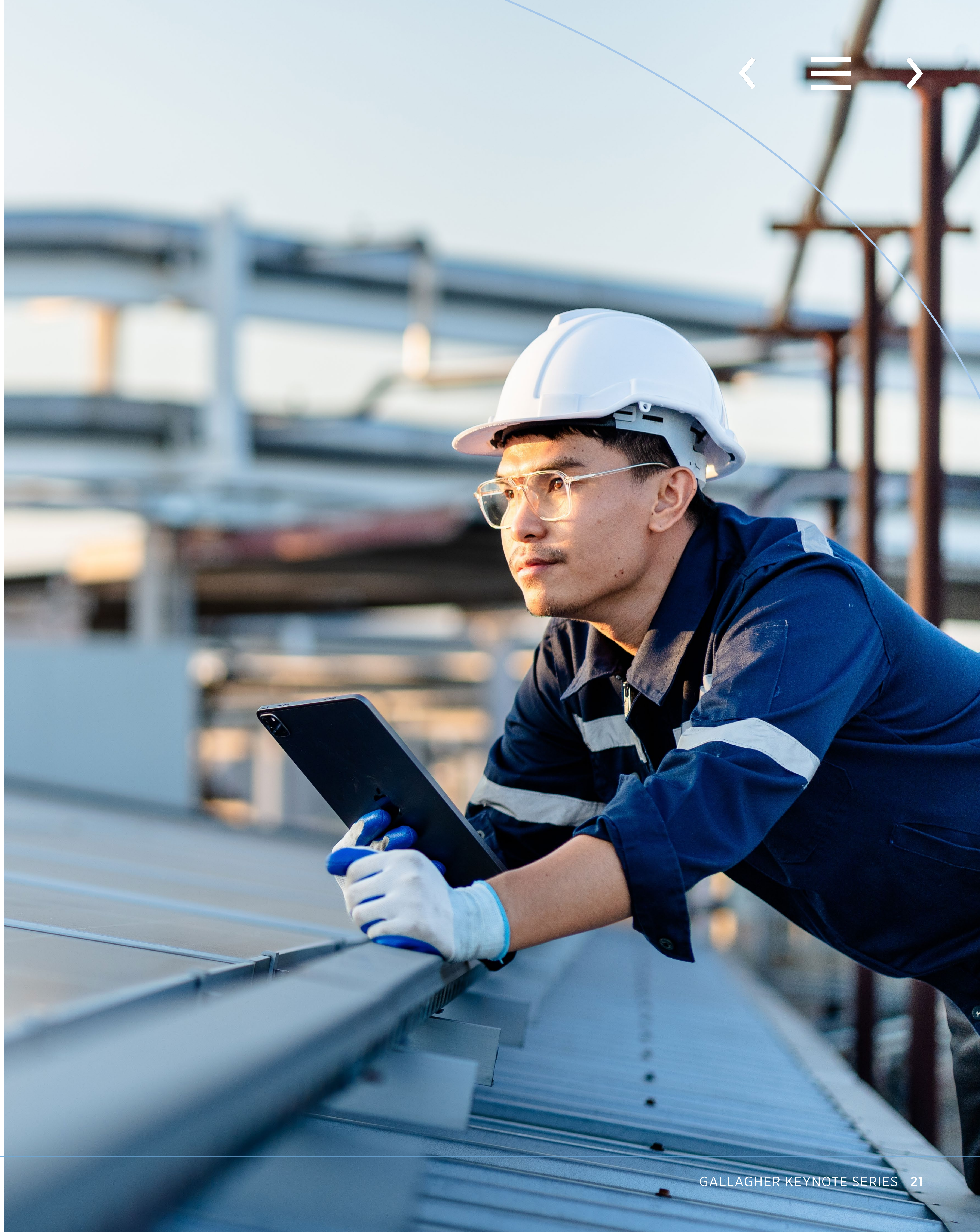
According to the International Labour Organization (ILO), the structural transition to net zero is best promoted by reskilling workers and supporting and incentivizing the move to greener, more formalized jobs using social protection systems.[17]

Insurance companies have a role to play, both directly by providing social protection such as health benefits and disability protection and indirectly by offering incentives to employers that support workers — for instance, rewarding employers with premium discounts where they can demonstrate progress towards just transition-related sustainable development goals (SDGs).

"Social protection is typically provided by the state and employers, but there is a growing role for the insurance industry," says Craig Churchill, Chief of the ILO's Social Finance Program. "We need to consider the role of finance and insurance in this transition and what companies and governments should do to prepare people for the transition and provide social protection."

He adds, "It appears that there are not enough measures in place to support this pathway. Insurance companies can incentivize a just transition and use their influence to positively impact the economy. It's not about refusing to insure but about moving in the right direction and seeing improvements."

"Insurers should assist their customers in achieving net zero, and what that looks like will vary depending on the region they are in," says Mia Seppo, Assistant Director General for jobs and social protection at the ILO. "In developed regions it is about incentivizing and providing support to workers in businesses. In developing regions, it is about making insurance accessible to households and enterprises to reduce risk exposure."

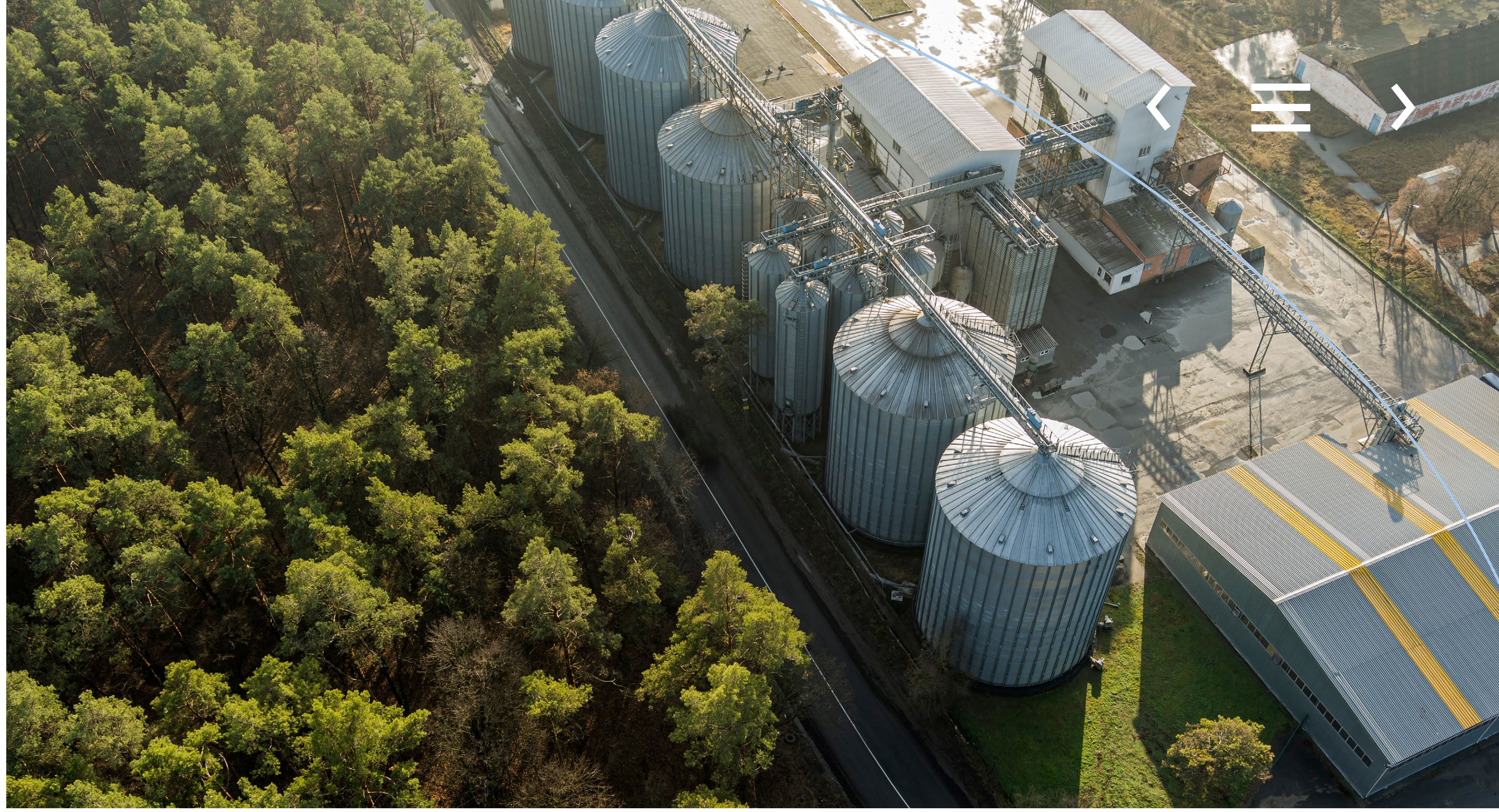


Fairer distribution of climate change costs?

In the context of the global north-south divide, social protection is a mechanism to more fairly distribute the cost of climate change, especially for communities that face physical climate extremes in addition to transition risk impacts.

“Leaving no one behind can mean different things to different people,” says UN SDG Academy’s Lorcán Hall. “Some may think it only applies to those who are losing something in the energy transition, but it’s much broader than that. Significant inequalities in society need to be addressed for a just transition. Legacy issues must be considered as well.”

The provision of social protection is an essential aspect of any just transition and one in which the insurance industry can play a role, alongside governments and employers.



Supporting transition journeys

The insurance industry’s role in supporting commercial clients on their transition journeys through risk transfer, prevention, and mitigation solutions is another well-documented aspect of the transition to net zero.

The opportunities the transition presents could double the size of the London insurance market, according to the broking body London & International Insurance Brokers Association (LIIBA), in growth sectors such as complex infrastructure development and carbon offsetting.[18] It argues that the industry, and brokers more specifically, can incentivize the net zero transition “through the scale of the London market” by providing “stronger price signaling, reducing costs for low climate risk.”

But industry-wide strategy and action are needed for climate transition opportunities to happen. Risk and insurance managers have expressed frustration at what they consider to be a lack of support from the insurance industry for companies making progress on their individual journeys to net zero.[19]

While there are examples of insurance products that offer a discount for companies that achieve SDG or ESG targets, for instance, the approach is ad hoc and needs to be more joined up to make any real impact.

Limited progress in harnessing insurance for achieving net zero

In an October 2019 whitepaper, the Federation of European Risk Management Associations (FERMA) pointed out the key influence insurance has on the net zero transition and warned it wasn't enough.

"Companies will be under pressure to show their progress to carbon neutrality, but lack of sufficient risk transfer will slow investments in innovative technologies as more risk must be carried by the enterprise," said FERMA.

While a few examples of innovation support net zero within the insurance industry — such as SDG-linked insurance policies — remains a niche service available only within a specialty marketplace. Nevertheless, some progress is being made.

In October 2022, the insurance mutual association International Cooperative and Mutual Insurance Federation (ICMIF) launched an insurance SDG calculator that the Swiss Re Institute developed to measure the sustainability impact of insurance SDGs within individual company insurance portfolios and business operations.

"The big companies are beginning to realize that linking their underwriting strategy to the SDG calculator would be beneficial," says Shaun Tarbuck, CEO of ICMIF.

"By doing so, they can change their products to be more sustainable and live up to the SDGs through their underwriting strategy."

Insurers can be creative in how they encourage the right behaviors with regard to a just transition. Far from being solely philanthropic, insurance companies will benefit financially because their incentives should help reduce the underlying risk.

"In planning documents for renewable projects in the UK, there is often a requirement for 50% of the workforce to be sourced locally," says the ECITB's Andy Brown. "However, many companies meet this by hiring bus drivers, caterers, landscape gardeners, etc., and not the more technical workforce. To address this issue, there needs to be more prescriptive and controlling measures at the consent order level."

He continues, "Asset owners could receive tax breaks and insurance premium breaks for prioritizing local talent, for instance. Managing competence in a cohesive and peer-to-peer manner is a more mature approach, and there could be an insurance premium incentive."

The insurance industry has an important role to play in supporting the transition to net zero. By incentivizing the right behaviors and offering solutions for reskilling and social protection, insurers can positively impact the economy and help bridge the skills gap, bringing in new sources of premium to the industry in the process.

Opportunities for public-private partnerships and microinsurance solutions

The insurance industry plays an essential role in providing risk financing for weather-related catastrophes through traditional property catastrophe re/insurance coverages, public-private initiatives, and microinsurance solutions.

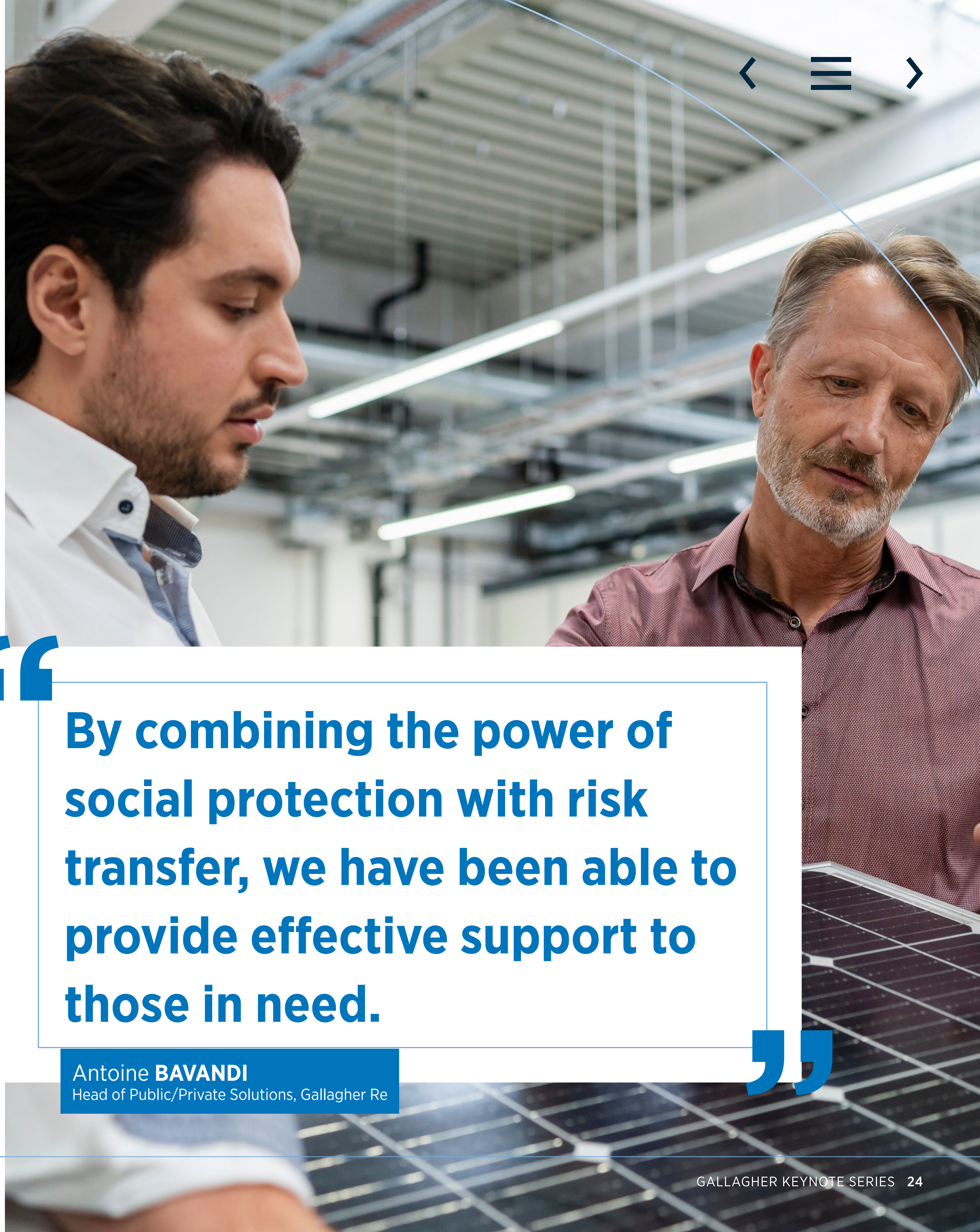
Now, more specific risk transfer solutions are being developed in response to the challenges posed by the transition to net zero. Some of the more innovative solutions encompass elements of social protection.

“By combining the power of social protection with risk transfer, we have been able to provide effective support to those in need,” explains Antoine Bavandi, Executive Director — Head of Public/Private Solutions, Gallagher Re.

“In Morocco, [after the 2023 earthquake] we mobilized a reinsurance product for the public Solidarity Fund, resulting in a significant payout when it was most needed. This funding went directly towards assisting those affected,” he says. “Our strategy of mobilizing liquidity before disaster strikes has proven to be a game-changer, and we believe that public-private partnerships are key to achieving lasting results.”

Public-private partnerships and microinsurance solutions can help tackle protection gaps and ensure financial safety nets are in place for workers and communities in more vulnerable regions.

“It is one thing to design insurance, reinsurance, and contingency funds for disaster events. It is another thing to make sure the money flows to the beneficiaries in affected areas,” says Bavandi. “To address this challenge, we rely on existing social protection schemes or registries of the poor and vulnerable to ensure that the money is targeted towards those who need it most. We also emphasize the importance of transparency to generate efficiency and timeliness of payouts.”



“By combining the power of social protection with risk transfer, we have been able to provide effective support to those in need.”

Antoine **BAVANDI**
Head of Public/Private Solutions, Gallagher Re