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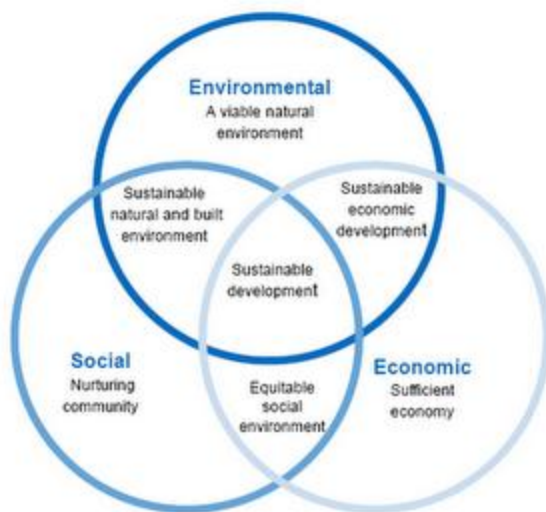
Insurance and Sustainability

2011 Writing Contest

## Definition and Explanation of Sustainability and its Importance

Sustainability is a term that refers to the “overall capacity to maintain a certain process or state indefinitely” (Risk Management Insurance and Sustainability), and for businesses is often an ongoing goal and process as it can be difficult to achieve and requires making changes in business practices. Issues arising in the 1980’s, such as the progressive deterioration of Earth’s natural environment and resources, were recognized as consequences of human activity from short-term gains of the past. These sustainability issues are characterized by short-term problem-solving which may have posed a success or solution initially, but led to a downfall because the process or state of success was not possible to endure forever. The Brundtland Commission came up with the term ‘Sustainable Development’ in 1987 to explain an ideal condition where development satisfies present needs “without compromising the ability of future generations to

meet their own needs” (Risk Management Insurance and Sustainability). This concept is considered in three equally important pillars of sustainability which are Environmental, Economic, and Sociopolitical.



the environment to meet future needs, and as a result begin reducing carbon footprints to benefit the environment. These businesses are often rewarded with highly regarded reputations, increased profits, and competitive advantages.

The sustainability of the marketplace and the planet are affected by all businesses and individuals, whom each contribute to “enrich[ing] the quality of life of present and future generations” (Locke 2011) by meeting the triple-bottom-line. Businesses that sustainably balance the three pillars through the triple-bottom-line concept create value for their customers and investors, preserve

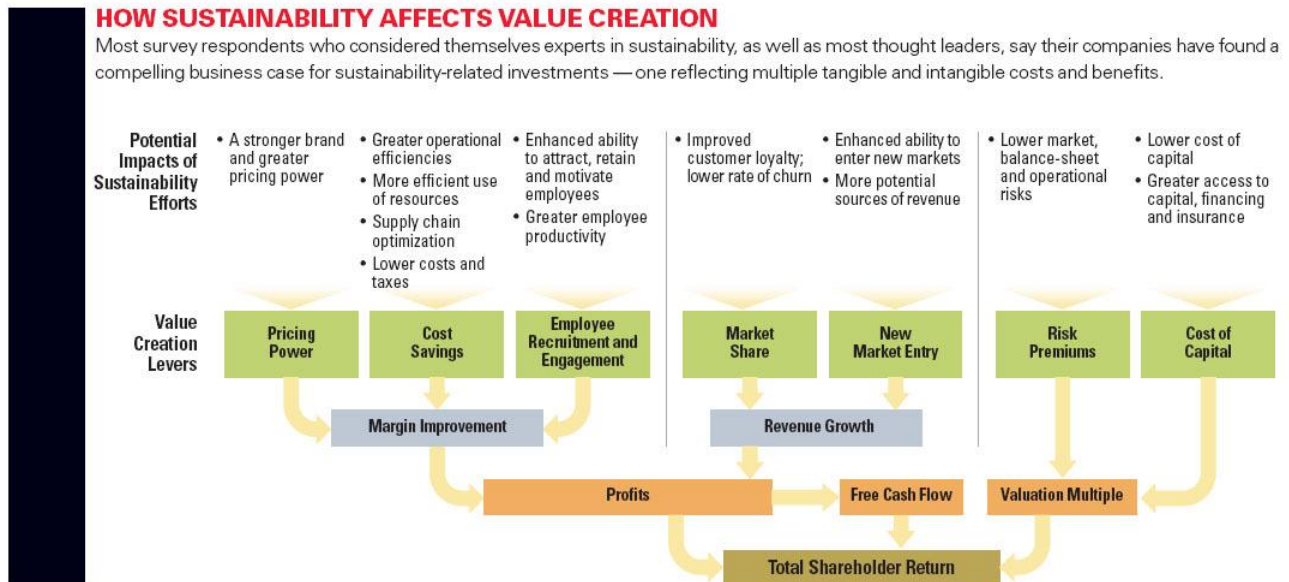
The production of products and services in unsustainable businesses in the past combined with booming population growth has had lasting negative impacts which threaten human health and the environment throughout the world. Awareness about the importance of sustainability as well as collaboration between individuals, businesses, and countries internationally are critical to reducing carbon footprints that have already been left on the Earth. Sustainable production of products and services can be difficult because they do not negatively impact the environment, economy, or society (Sustainable Business 2011) in any way, currently or in the future. Additionally, it is important because “given the dual role of insurance companies as investment vehicles and fiduciaries, their duty to take sustainability into account is particularly acute. The unique position that the insurance sector has in terms of sustainability topics is also revealed in insurers’ balance sheets, as both assets and liabilities are affected in interdependent ways. Thus, the leverage insurance companies stand to gain by incorporating sustainability topics is considerable” (West LB 2004).

## Sustainability in Insurance and How it Affects the Industry

Sustainability is particularly important in the Insurance industry in the fields of Risk Management and Underwriting. The foundation of insurance is based on the transfer of risk to protect individuals and businesses from unexpected or unplanned losses, so when sustainability issues arise from unsustainable processes or states of the past, Insurance or Reinsurance companies must pay for those losses. Sometimes these losses were fortuitous even to the Insurance company because the perils causing the loss were entirely unknown to exist, or they are occurring with an unexpectedly higher frequency. Insurance and Reinsurance companies provide resilience to individuals and companies experiencing these unexpected losses or that have unsustainable practices. This requires Insurance companies to always be a few steps ahead, constantly updating and changing their policies and coverage to incorporate and address sustainability issues that could potentially arise.

Another explanation for why Insurers should care about sustainability is through Swiss Re's acknowledgement that "sustainability is not just a nice-to-have for Swiss Re. Unsustainable trends threaten resources and potentially augment losses, which is why we foster the principles of sustainability with all our stakeholders" (Risk Management Insurance and Sustainability).

More and more companies and investors are taking notice "that climate change carries significant economic implications for shareholder value. The particular relevance for insurers is due to the close correlation between underwriting losses and losses in the value of capital market investments". The value created is displayed in the chart below. Insurance companies are experiencing more frequent and costly losses, some of which threaten an insurer's underwriting profitability, allowing us to conclude that "a systematic approach to risk management which incorporates pricing, selection and research is essential" (West LB 2004).



Additionally, “the payoff of sustainability-driven management” has many intangible payoffs and strategy benefits such as process improvements, employee engagement, developing a competitive advantage, improved resource efficiency and waste management, the ability to innovate, and the opportunity to grow. The companies that have embraced this view of sustainability were the “highest performing companies in the study” when compared to businesses that are adopting sustainability views and practices in a more gradual and cautious process. The debate is whether sustainability will eventually become the core of business decision-making and a business’s ability to grow, or if it is already at the core, as some businesses (sustainability embracers) are handling it (Sustainability: The “Embracers” Seize Advantage).

### Insurance and Reinsurance Organizations Addressing Sustainability Issues

To avoid numerous and costly losses that could arise from sustainability issues in emerging market countries while also acting in the best interest of the community, shareholders, and the environment, Insurance and Reinsurance Organizations often focus on several issues; especially those related to climate, social responsibility, and microinsurance.

#### ➤ Climate

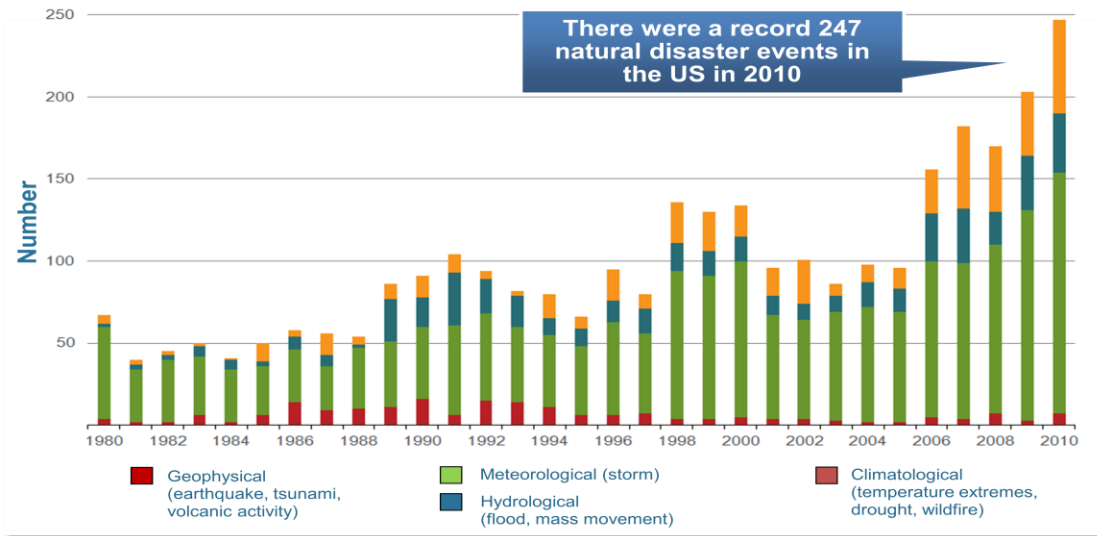
The president of the Pew Center on Global Climate Change, Eileen Claussen, suggested that “perhaps no other industry is more exposed to the financial risks of climate change than the insurance industry, but the unique risks faced by the industry also present it with an opportunity to take a leadership role in responding to the climate challenge” (Risk Management Insurance and Sustainability). While virtually every industry is affected by the financial risks that climate change brings, it is becoming an increasingly hot topic for Reinsurance companies. The climate has changed drastically in the past 10 years; increasingly concentrated emissions of greenhouse gases from certain businesses and technology are causing a rise in Earth’s temperatures, which can be harmful to human health and the environment (Greenhouse Gas). Additionally, as shown in the charts below, natural disasters have increased tremendously in the past 10 years, bringing expensive and reoccurring losses to Insurance and Reinsurance companies. Not only are these events increasing, but so is their severity. 8 of the 12 largest natural disasters in United States history have occurred since 2004 (Hartwig 2011). So now, in 2011, what are Insurance and Reinsurance companies doing to address these issues?

Many businesses are “going green”, or have begun adopting environmentally friendly activities to reduce harm done to the environment. A few companies have taken those leadership roles Eileen Claussen mentioned, and have developed rather innovative products and services that address sustainability issues. One of these companies, Munich Re, has taken initiative by launching projects concerning climate change, involving other organizations in the research and quest to find new technologies, and set up Dii GmbH, which focuses on desert energy. Their heavy involvement with research in addition to their collaboration with scientists and other organizations has helped them to produce new climate change products and develop risk transfer solutions (Kabish).

Swiss Re, another leader in sustainability innovation in insurance, is focusing on ways to extend coverage to emerging countries as well as adapting to climate change. “Insufficient insurance cover is a major challenge for emerging markets and a persistent development obstacle. Over the last few years, we have developed a range of products that improve insurance

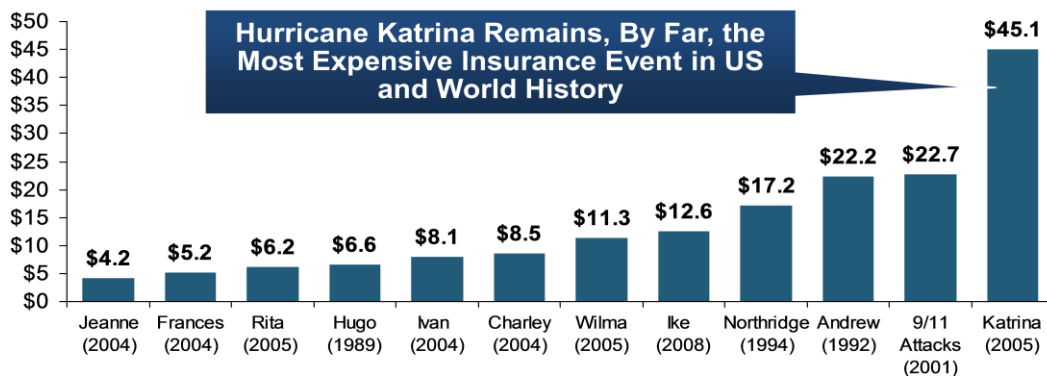
## Natural Disasters in the United States, 1980 – 2010

Number of Events (Annual Totals 1980 – 2010)



## Top 12 Most Costly Disasters in US History

(Insured Losses, 2009, \$ Billions)



8 of the 12 Most Expensive Disasters in US History Have Occurred Since 2004;  
8 of the Top 12 Disasters Affected FL

protection against key risks such as earthquakes, windstorms and droughts”, one of which helps assess how cost-effective various adaptation measures are. Swiss Re has been finding and funding solutions that help societies in adapting to climate change, and mentions that “striking up partnerships with governments and public-sector organisations has been a vital component of these efforts” (Creating Sustainability Solutions).

It is important for Reinsurance companies to pursue and research climate change issues in order to better serve businesses and individuals whom reap the benefits of Reinsurance; but participation is also strategic because it helps define covered losses and put into effect global regulations that make climate risks less variable. Climate risks are open for much interpretation, so attending annual meetings and combining knowledge of these issues makes these risks more clear.

### ➤ Social Responsibility

Organizations are socially sustainable when they help benefit the community and increase the quality of life. This can be in a variety of ways, such as volunteering, offering internships to students, encouraging continuing education, and providing training to employees. They must take into account their employees, customers, and reputation.

Andrew Tunnicliffe, chief operating officer of Aon Global Risk Consulting, brings to our attention a new idea in corporate social responsibility for Insurance and Reinsurance companies. “The insurance industry has the power to influence and create a greener society. Green insurance products could include reduced premiums and enhanced coverage for buildings constructed to withstand extreme weather events; pollution legal liability and remediation cover; specialist insurance for renewable energy projects; and health insurance products that reward healthy lifestyles” (Risk Management Insurance and Sustainability). Reducing premiums provides an incentive for businesses to move towards greener practices or take a more active role in green issues. Good citizenship will result from the benefits that Insurance companies can offer, and ultimately helps the world move forward more sustainably.

Sustainability has been incorporated into company policy and made a priority in some Reinsurance companies, such as Munich Re. Munich Re impacts the economy by investing in companies that have very sustainable business practices, are working to reduce greenhouse gas emissions, or concern themselves with the issue of global warming (Kabisch). By pumping this capital into the real economy, they are contributing to the growth and prosperity of many companies. Investing in companies that take an active role in sustainability issues of environment, climate, or renewable energy is a great reward for those businesses and has been very profitable for Munich Re.

### ➤ Microinsurance

Microinsurance is, in literal terms, “small insurance”; small caps, small coverage, small premiums. It is typically offered to low-income businesses or people to aid in managing health or property risks, help people grow their businesses, and protect them from natural disasters in emerging market countries. Essentially, it is Insurance designed for a low-income market. Microinsurance providers at times receive funding from organizations interested in expanding

the network of people who can enjoy the basic protection insurance offers. Microinsurance works because it utilizes large risk-pooling to ensure financial protection for those who are exposed to risk, and access to a Reinsurance company provides a support structure for improved governance. It is beneficial to Insurance companies because they are contributing to the improvement in the quality of life in poorer countries, but it also provides an opportunity “of great potential growth and profitability as insurance markets in developed countries become saturated and growth prospects limited”. Microinsurance also offers an opportunity for growth, “as many of today's microinsurance clients will be the middle class clients of tomorrow” (Microinsurance). “According to the Munich Re Foundation, of the 3 billion people who live on less than £1 [\$1.62] a day, fewer than 10 million currently have access to insurance” (Micro insurance), which also demonstrates how much room there is for Insurance and Reinsurance companies to grow in this area. Providing insurance for the poor is a form of social responsibility as well, and facilitates development of sustainable solutions to unexpected risks faced by poor people.

Richard Leftley, President of MicroEnsure, says “we offer our clients insurance because they face a huge number of risks every day. Without it, they have no safety net to stop them slipping back into abject poverty” (Micro insurance). Oftentimes, financially less fortunate people are forced to use their savings when unexpected loss strikes, making these people and their families more susceptible to losing everything they have. They do slip back into poverty sometimes, but the quality of life in these emerging market countries is improving as funding and insurance coverage expand.

## Opinion

I think Sustainability is an exceptionally important topic for Insurance and Reinsurance companies to focus on. If these companies are not already involved in developing sustainable practices and innovating in the areas of Microinsurance, CSR, and going green, they are falling behind. It is beneficial to others in the ways that it provides services to others that they cannot provide for themselves, keeps employees and customers happy, and moves towards practices of meeting today's needs without compromising the ability to meet future needs. Sustainability generates value for customers and investors, as reinsurance companies invest in green companies and customers do business with those same companies. It gives the sustainable company an excellent reputation, a competitive advantage, and the opportunity to innovate and grow. Sustainability also supports reduction in damage done to the environment from goods and services production, and promotes healthy business practices. Reinsurance and Insurance companies must face the devastating present and future consequences from unsustainable ways of the past, and they can begin by analyzing what has gone wrong before compared to what is working now. These companies serve as society's backbone for unexpected losses, and developing a new way to tackle these issues now is what will ultimately protect and better the future.

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