Policy options to reduce the climate insurance protection gap

Zurich’s feedback on the EIOPA and ECB discussion paper

Introduction

Zurich Insurance welcomes the paper presented by the European Insurance and Occupational Pensions Authority (EIOPA) and the European Central Bank (ECB) on “Policy options to reduce the climate insurance protection gap”.

We appreciate the opportunity to provide feedback on this valuable work and on this important topic – an area where Zurich has gained insights through serving people and businesses in more than 200 countries and territories worldwide. In addition to providing insurance protection, Zurich is increasingly offering prevention services, including those that enhance climate resilience and help close the protection gap.

Summary

We welcome EIOPA’s and ECB’s acknowledgement of the central role of private insurance in coping with climate-related risks and impacts, by providing financial protection to individuals and companies, fostering the uptake of resilience and adaptation, as well as partnering with public authorities.

In considering ways to tackle a growing protection gap, the paper focuses on insurance penetration, financial risk transfer and the role of public sector in risk transfer solutions. Insurers, including Zurich, will continue to improve their risk modelling and assessment capabilities to support better pricing and to help tackle the climate-related protection gap. However, for these risk transfer solutions to be sustainable over the long-term, more focus will also be required on the development and delivery of effective and comprehensive disaster risk reduction measures. Insurability will be increasingly contingent upon implementation of resilience and adaptation measures, and it is important that policy options to support investment in those measures across Europe are considered alongside risk sharing public-private partnerships.

The insurance industry and the public sector should play supporting roles. Insurers can provide data-driven insights, advice, and incentives to help their customers improve their resilience. The public sector, in turn, should foster adaptation at European, national, and local level through overarching and strategic policies (e.g. the EU Strategy on Adaptation to Climate Change), planning rules, improved availability of data and collaboration with the industry on individual projects.

To effectively tackle the climate insurance protection gap, Zurich recommends the following actions:

- enhancing resilience and adaptation as first line of defense, to avoid losses as well as to preserve the affordability and availability of insurance; insurers can play an important role by leveraging their expertise to advise customers and public authorities on risk prevention and management;
- encouraging greater involvement of the public sector through informed resilience and adaptation policies, planning rules and support for targeted investments;
- raising risk awareness among households, companies, local communities and governments on climate risks and impacts, and the benefits of appropriate risk prevention; greater awareness should be promoted also on the role of insurance; the public sector, in particular, should receive appropriate upskilling and know-how building to work with insurers on resilience and adaptation;
- establishing public-private partnerships (PPPs), which preserve risk incentives and risk-based pricing as well support investments in resilience;
- embedding an “ecosystem approach” in policymaking and regulatory actions, by streamlining and connecting existing and future workstreams, including through collaboration among European institutions, as well as with the insurance industry (e.g. EU Commission initiatives and the ongoing work of the Climate Resilience Dialogue).

Our detailed analysis focuses on Layer 1 (on the role of private insurance) and Layer 3 (on the role of PPPs), as per the ladder approach proposed in the paper.

We would be delighted to discuss these points in more detail.
Enhancing resilience and adaptation as first line of defense

- Private insurance should not be considered as “the first line of defense to cover losses from climate-related natural disasters”, as the paper postulates (p. 3). Traditional insurance products are primarily designed to aid the recovery process. An appropriate risk management approach implies: 1) loss prevention, through resilience and adaptation measures as a first line of defense, and 2) insurance as second line of defense on protection and relief from unavoidable financial losses. More resilient communities, commercial and individual customers will help extend insurance coverage. This will also contribute to reducing the share of economic losses from natural hazard events borne by the public sector.

- Insurance companies have an important role to play beyond the risk-based conditions or incentives in insurance policies (“impact underwriting”) outlined in the paper. Insurers can deploy expertise in assessing the exposure to climate risks and estimating the potential magnitude of their impacts to advise companies and local communities on how to best prevent and manage future risks. Through Zurich Climate Change Resilience Services we support commercial customers and other companies to strengthen the climate resilience of their operations by combining expertise on risk engineering and climate data science.

- Resilience and adaptation is relevant for the entire infrastructure and ecosystem. The buy-in of the public sector at local, national, European and international level is critical to deliver effective resilience and adaptation policies, planning rules (e.g. building codes, zoning laws, etc.), grants and direct investments in resilience and adaptation projects (e.g. installation of early warning systems in flood-prone areas). The public sector can provide and facilitate investments in new and/or improved infrastructure, requiring resilience and adaptation as pre-requisite in the design phase (e.g. through Green Public Procurement criteria for public buildings). So-called “build-back-better” measures can also be used to strengthen communities, companies, and households following a disaster.

- At local level, insurers can provide public officials with science and data-driven overviews to inform policies and investments. For instance, Zurich Resilience Solutions is advising the Madrid City Council on identifying and quantifying the hazards associated with heat to define adaptation measures to be included in the climate resilience plan of the city. Following the same risk assessment methodology adopted with commercial customers, our experts have analyzed the exposure of school children to heat and combined this with insight across a broad range of vulnerabilities (e.g. lack of outdoor space, low-income neighborhoods, children with chronic diseases etc.) to create impact scenarios with quantitative and qualitative assessments, and with projections of their evolution in different time-horizons. Zurich Resilience Solutions then recommended adaptation measures to complete the risk assessment process.

Raising risk awareness

- Raising awareness among households, companies, local communities and the public sector on exposure and vulnerability to-, and on potential losses from climate risks, as well as on the effectiveness of risk reduction measures is the first step towards triggering actions conducive to greater resilience and adaptation. The paper only briefly mentions this aspect while commenting on the features of insurance products and the obstacles to insurance penetration (p. 19).

- Insurers can help to bridge the information gap. Improving the accuracy of risk assessment and modelling is crucial to better estimating the frequency of climate-related catastrophes and understanding the potential magnitude of their impacts. This requires closing data gaps in terms of tools and methodologies. Hence, data issues are important at each layer of the ladder presented in the paper.

- In particular, the disclosure of publicly-owned data on risk exposures and forward-looking developments of risks trends would help in risk assessment, future scenario planning, and inform decision-making at private and public level. Public authorities should disclose this government-/public entities- owned data through a single, publicly accessible database. EIOPA is in a good position to steer and lead initiatives within the public sector on the collection of publicly-owned exposure data.
Greater risk awareness also requires targeted communication tools directed towards individuals and communities. Messaging and dissemination methods must be tailored to different audiences, and multiple tools are needed. Technologies, especially low-cost and open-source, as well as early warning systems, play a particularly important role in fostering flood resilience and adaptation.

- These tools could be useful in Europe’s flood-prone areas, where the “Bernd” flood in 2021 (hitting Germany, Belgium, Luxembourg, and the Netherlands) and the floods in Emilia Romagna (Italy) in May 2023 – just to name a few examples – have been wake up calls to the fact that floods and the relative lack of preparedness are not specific to emerging economies, but represent major threats in the EU. Based on our review of the “Bernd” flood, we have put forward a number of recommendations, including the importance of improving the early warning systems, creating a “culture of risks” and raising risk awareness among decision-makers and the public.

- Open-source data modelling tools providing easy-to-use and easy-to-understand overviews of the exposures to disasters from natural hazard events can also help, and we welcome recent initiatives of EIOPA in this field with the launch of the CLIMADA-app. Another valuable example of the use of data for raising risk awareness is represented by our Natural Hazards Radar, a free online service enabling basic understanding on the exposure to natural hazards in Switzerland: a map, which belongs to the cantons, is integrated in an easy-to-use digital tool, allowing users to access a unique screen showing the exposure to multiple hazards of a specific area, by typing a simple address.

We also welcome science-based standards such as the recently presented technical guidance on adapting buildings to climate change, we have contributed to.

We fully endorse the paper’s call for information campaigns to raise awareness about adaptation measures and their potential effectiveness in risk reduction (p. 19). The support of public authorities is crucial to fund, organize and conduct these campaigns.

Information campaigns should aim at raising awareness of the role and basic functioning of insurance, targeting also key public officials in national and local governments.

In addition to this, public authorities could be instrumental to:

- support a change of mindset in the broader society: current general expectations are that 1) buying insurance is enough to ensure protection from risks; and 2) when a big disaster occurs it is first and foremost up to local entities and/or governments to step in and provide immediate relief, financial coverage, and reinstatement of the pre-disaster situation; as opposed to this, society should accept the idea that dealing with climate change requires shared responsibility between public sector, insurers and individuals, prevention, and availability to adapt;

- help deconstruct psychological biases (e.g. optimism, poor understanding of numerical risks), which could inhibit uptake of resilience efforts in the first place, and insurance coverage as a second step.

Establishing Public Private Partnerships (PPPs)

- Insurance penetration is another area where insurers and public entities can join forces to extend coverage in cases where risks are uninsurable or too costly to insure at market conditions. Public-private-partnerships (PPPs) can provide effective solutions to pool and integrate different expertise, as well as to share risks, costs and responsibilities between public entities, insurers, and policyholders.

- According to the paper, PPPs are intended as being more commonly adopted to address low frequency and high-impact disasters from natural hazard events. Our experience suggests, however, that PPPs can be viable opportunities to extend the coverage also for low impact and high frequency hazards, especially in physically and socially vulnerable contexts, depending on the specific needs of communities and/or individual customers.

- We welcome the paper’s emphasis on the need for PPPs to embed preconditions on pro-active measures for risk mitigation and adaptation (p. 27). Without these elements, and the adoption of risk-based pricing, sharing pools can be exposed to moral hazard and prove less effective to address a widening protection gap.

- PPPs cannot be considered as the sole and definitive solution for closing the climate protection gap. Adequate policies and investments in risk prevention and adaptation should be enacted at EU, country
and local level to strengthen communities vis-à-vis the increasing frequency and intensity of disasters from natural hazard events and make these PPPs sustainable.

- We recommend leveraging insight from France where a portion of the premiums raised by insurers in the NatCat scheme is allocated to the major public natural risk prevention fund (Fonds de Prévention des Risques Naturels Majeurs - FPRNM), known as the “Barnier fund”), financing measures to prevent risks from extreme natural events. The NatCat scheme is based on flat premiums with fixed rates set by law, and calculated on the premium of the basic private property insurance. We are supportive of this fund as it allows interventions in local communities (e.g. management of waterways and communication campaigns), as well as among individuals and companies.

- Also, we welcome the fact that the Mission of insurance companies for knowledge and prevention of natural hazards (Mission Risques Naturels - MRN) involves all stakeholders when it comes to mitigating risks by: 1) acting as technical interface between the insurance sector and the various stakeholders in the management of natural risks; 2) increasing knowledge of natural risks and evaluating public prevention systems; 3) providing insurance companies with tools to analyze risks exposure.

- Based on our experience in a broad range of markets worldwide, we conclude that effective PPPs should have the following characteristics:
  - Pricing must reflect the underlying risks to avoid free riding and moral hazard. The funding mechanisms may introduce some forms of subsidization to preserve the affordability of the insurance policies, especially in areas of lower-income levels and/or high exposure to risks. Subsidies should not hide the true level of risk, but help customers afford the corresponding premiums (e.g. through vouchers or tax incentives).
  - Public authorities, insurance companies, and policyholders must all retain responsibility and “skin in the game” to avoid moral hazard, as well as to generate enough incentives for prevention.
  - Insurers should remain the interface to customers to provide cost effective insurance cover and risk management expertise, and to handle claims.
  - Insurance policies should incorporate “resilience-by-design” and “build-back-better” conditions and services: insurers should be able to impose conditions on how goods are procured/replaced, and properties built/rebuilt. Insurers can also offer advice services to reduce the exposure and vulnerability to covered risks and to enable customers to better manage impacts when disasters hit.
  - The governance and set up must be as much as possible on an equal basis, with both private and public partners represented in the various operative and steering committees to ensure alignment and commitment; independence from individual sectors is also key, as PPPs cannot be seen as a channel for specific sectors pushing through their business goals and agendas.
  - Public funding and political support should be adequate and sustained over time, and red tape reduced as much as possible to ensure fast, efficient, effective and long-standing response to communities’ needs.

- Finally, we support efforts to foster greater cooperation on resilience within the EU. Whilst we see the merits of developing an EU wide scheme – as outlined in the paper – the establishment of well-functioning country level PPPs should be prioritized.

---

**Zurich Insurance Group (Zurich)** is a leading multi-line insurer serving people and businesses in more than 210 countries and territories. Founded 150 years ago, Zurich is transforming insurance. In addition to providing insurance protection, Zurich is increasingly offering prevention services such as those that promote wellbeing and enhance climate resilience.

Reflecting its purpose to ‘create a brighter future together’, Zurich aspires to be one of the most responsible and impactful businesses in the world. It is targeting net-zero emissions by 2050 and has the highest-possible ESG rating from MSCI. In 2020, Zurich launched the Zurich Forest project to support reforestation and biodiversity restoration in Brazil.

The Group has about 56,000 employees and is headquartered in Zurich, Switzerland. Zurich Insurance Group Ltd (ZURN), is listed on the SIX Swiss Exchange and has a level 1 American Depositary Receipt (ZURVY) program, which is traded over-the-counter on OTCQX. Further information is available at [www.zurich.com](http://www.zurich.com).