United Nations | Committee of Experts on Public Administration 2024

Regulating and reforming the insurance industry to combat climate change*

Summary

Years of large catastrophe losses due to more frequent and severe climate-related weather events have led to insurance coverage gaps in many countries, with devastating impacts for governments and individuals, especially vulnerable groups. Increased collaboration between governments and the insurance industry is required, paired with accelerated regulation and reform, to better mitigate the risks associated with climate change. Enhancing the capacity of governments at all levels to analyse risks, incentivize investment in resilience, prevention and rehabilitation, and explore the development of tailored financing mechanisms, including parametric approaches to insurance, is seen as urgent.

Recommendations

The Committee recommends that the Council:

Express concern at the limited capacity to foresee and build resilience against the diverse challenges originating from multiple shocks in many countries, and *call for* a rapid upgrade of the risk management function in government and its integration into Sustainable Development Goal-related coordination mechanisms at the highest level (Paragraph 8).

► See ECOSOC resolution 2024/L.14

* Excerpt from Committee of Experts on Public Administration, Report on the twenty-third session. See Official Records of the Economic and Social Council, 2024, Supplement No. 24 (E/2024/44-E/C.16/2024/9)

The Committee of Experts on Public Administration is a subsidiary body of the United Nations Economic and Social Council (ECOSOC) advising on issues related to governance and institution-building for the achievement of the Sustainable Development Goals.

Discussion

Public-private partnerships in insurance

The Committee observes that the insurance industry plays an important role in partnering with governments to measure, monitor and mitigate the impact of climate risks. Its role in estimating risks and helping governments to mitigate losses owing to disasters makes it important for governments to ensure that the insurance market is regulated in ways that work for all stakeholders.

Climate change has exacerbated the gap between the amount of insurance coverage provided by the industry and the amount of harm that individuals and households suffer owing to catastrophes, such as floods, droughts, storms, wind and extreme heat. That growing protection gap is especially pronounced for vulnerable groups and communities and can severely undermine government efforts to protect public assets. It is also important for governments to provide some oversight to ensure that insurance companies maintain a presence in local markets, provide insurance at reasonable prices and plan for situations in which governments might need to adjust zoning, regulations or other policies to help to mitigate damages before climate disasters strike.

Such programmes will involve collaboratively sharing the risk burden with private insurers, providing a financial backstop for extreme events and ensuring that resources are efficiently mobilized to address the economic fallout of disasters. By engaging in partnerships with the insurance industry, governments can enhance the overall sustainability of the insurance market and generate additional capacity to support new insurance products.

In addition, reinsurance companies provide insurance to the insurance companies themselves and are therefore a backstop for the industry. Governments need to better understand that sector and help to ensure that it is functioning as a true backstop to the retail insurance sector. This can require governments to step in to regulate and oversee the reinsurance industry, to ensure that the private sector does not withdraw from a region or fails to maintain reasonable coverage for the most vulnerable.

Innovative insurance products and financing

The Committee agrees that governments should actively encourage the development and use of innovative insurance mechanisms to cope with climate risks. This includes supporting the use of innovative products and approaches, such as parametric insurance, micro-insurance to support crops for small-scale farmers, and specific types of green bonds, catastrophe bonds and other measures. Those mechanisms will provide opportunities to attract capital from a broader pool of non-traditional investors, creating an additional source of financial support for climate risk insurance capacity.

Governments can also multiply the benefits of partnership with the multi-trillion-dollar insurance sector to advance the Sustainable Development Goals through, for example, investment that is environmentally sustainable, reduces greenhouse gas emissions and protects natural capital. Harnessing those assets for environmental purposes can help to reduce the number of climate disasters.

Greater transparency from insurance companies

For public policies to work effectively, it will be critical to foster a better understanding of the protection gap in climate risk insurance. Regulators should require insurance companies to disclose more information about who is being covered against critical natural hazards and about the premiums being charged. This will allow governments to clearly identify where the gaps are most acute and devise instruments to address market failures.

The insurance industry maintains the largest databases on risks, as well as actuarial and historical data, but it is difficult to ensure that reduced climate risk is reflected in lower insurance pricing. Proactive disclosure can enable governments to quantify the impact of public investment in new resilience measures, such as flood barriers or storm drainage, on the risk premiums being charged.

Regulators should also ensure that insurance companies improve the quality and scope of their routine climate disclosures. Insurance plays a critical role in the operation of many types of carbon-emitting activities, including the fossil-fuel industry itself. Detailed disclosure of the climate impact of insurers' underwriting activities, both directly and indirectly, can help to foster a more rapid transition to a low-carbon economy.

Better climate forecast data to assess risk

Governments are urged to conduct thorough macro risk assessments using the most recent data and forecasting relating to climate change. Such a proactive approach can ensure better preparedness, allowing for informed decision-making and the development of targeted risk management strategies. This requires a shift in mentality towards an open-data approach by which insurers are sharing data routinely and otherwise make their data easily accessible to governments.

By leveraging advanced climate data, governments can identify emerging risks, assess vulnerabilities and formulate adaptive measures to mitigate the impacts of climate change. Thorough risk assessments are crucial for developing resilient infrastructure, enhancing early warning systems and implementing effective climate adaptation strategies.

Product innovation in climate insurance

The regulatory system for insurance markets often makes it difficult or costly for insurers to experiment with new ways of delivering climate risk protection. Governments can incentivize innovation by establishing regulatory sandboxes in which new products can be tested and by providing financial support for initiatives that have the potential to become viable commercial products.

Specific innovations are needed to help cities to lower climate risks for critical structural assets, such as electrical grids and transport systems, cultural and historical assets, and homes, schools and hospitals. This requires partnerships to help to de - risk the assets themselves and ensure that they can be insured directly, and that cities have direct access to financial assistance in the event of disasters.

In developing countries, it is essential that governments and the insurance industry take steps to insure smallholder farmers against the risk of volatile crop yields owing to climate change. Insurance mechanisms, such as Pula, which provide microinsurance to millions of smallholder farmers, are able to protect against ruin in the event of major natural disasters.

Expanding the use of environmental-economic accounting

The adoption of the System of Environmental-Economic Accounting for estimating risks to ecosystems and biodiversity will allow insurance companies to measure the financial benefits of protecting ecosystems and biodiversity, ensuring a comprehensive approach to assessing the environmental impact of their operations and promoting sustainable practices within the industry.

International collaboration and regional risk pools

To adapt to the evolving nature of climate risks, cross-border regulatory frameworks, increased international coordination, and regulatory innovation are also required. The establishment of regional risk pools is one way to promote efficient risk-sharing and facilitate coordinated responses to shared challenges, while addressing the transnational impacts of climate change.

You can access the CEPA working group page for more information here.