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Collaboration: breaking the silos to mitigate risk

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Collaborative action is essential in order to create a coherent ESG strategy and meet the ever-rising expectations of governments and society. This is especially the case as we see a transfer of responsibility from government to the private sector, driven by a mixture of legislation and caselaw, which is increasing vulnerabilities and potential liability.

Climate activists have grown impatient with the lack of government action and are increasingly targeting the private sector, waging relentless campaigns against mining and energy businesses and their insurers in the battle to reduce fossil fuel use. Insurers need to understand how to manage these external pressures.

Outside the environmental arena, the Protect Duty legislation in the UK shows how quickly governments can shift major societal responsibilities from themselves to the private sector, potentially creating new liabilities.

The immediate scrutiny delivered by social media means that there is no hiding place for businesses and their insurers who are required to react to and plan for these challenges. Delivery is quickly measured against expectations and failure to meet those expectations is ruthlessly scrutinised – sometimes unfairly. Where the background noise on an issue is already intense and volatile, social media, especially when used maliciously, can quickly harness anger and turn it into agitation and violence.

CLIMATE ACTIVISM

Back in the environmental arena, the speed at which the focus of activist attention can move quickly from government to the private sector is well illustrated by the Urgenda case. This was initially lodged against the Dutch government on behalf of 886 Dutch citizens pressing for swifter and tougher action to fight climate change and mitigate its potential impact.

Royal Dutch Shell soon found itself in court accused by activists of not doing enough to reduce its carbon emissions – claims which the courts largely supported – and now the board of directors is having to defend itself against wider accusations that it has not acted appropriately to reduce the risks of damage to the climate.

This fits into a wider pattern says Duncan Strachan, Partner at DAC Beachcroft and class actions specialist:

"There is a definite trend towards the privatisation of risks that should be borne by government. The Urgenda case exemplifies litigation against a government being passed onto the private sector. The big question is where will it stop? It starts with the obvious targets such as fossil fuels and the oil and gas industry but will it then move onto other sectors?"

Insurers must rise to this challenge, says Toby Vallance, Partner and climate change lead at DAC Beachcroft:

"It is about understanding where the exposure is and it is not always obvious. Insurers have to review their position constantly, as what it is acceptable to insure and invest in is always changing. Coal was the first target, which was easier to move away from as it was already being phased out, plus oil and gas was the obvious alternative. The issue now is how you insure oil and gas, which is now seen as a target for activist pressure.

"Activist groups are getting more sophisticated and there is more litigation around the world. The pattern developing is activists suing governments for having inadequate net zero strategies first and then, if that is successful, they turn their attention to the corporates. Most recently, climate activists, including Friends of the Earth and ClientEarth have been partially successful in a judicial review claim against the UK government, with the court requiring the government to update its Net Zero Strategy to detail and quantify properly how its planned policies will achieve climate targets. It remains to be seen if we will see an uptick in activists bringing claims against UK based corporates.

"One feature of activist litigation is that it doesn't usually seek damages so there is no immediate impact on insurers, but there are serious consequential risks for D&O insurers. Activist shareholders could target firms with bold ESG statements who they suspect of greenwashing.

"There is also the potential of consequential climate change litigation, where corporate entities are being sued not because of their contribution to climate change but for failing to take account of the effects of climate change in how they operate their business, which has resulted in a loss. That is much harder to spot."

ESG OPPORTUNITIES

The response of the insurance industry and its partners shouldn't just be defensive, argues Vallance. He says there are opportunities to live out the bold promises of ESG strategies and deliver wider benefits to society, citing energy efficiency as one potential starting point.

The intense pressures on household budgets, and energy costs in particular, could present insurers with a chance to step forward with innovative solutions:

"There doesn't seem to be much progress on heating our homes more efficiently, especially with climate change and energy costs in mind. There could be a role for the insurance industry here. There needs to be a massive effort to get all the stakeholders to work together and get away from finger pointing … there needs to be an incentive for homeowners to move towards alternative heat sources."

This could be done through imaginative pricing of cover for homes with heat pumps, solar panels, high quality insulation and other energy efficient features. The move by Flood Re to encourage flood friendly reinstatement after a claim offers an example of how the insurance industry could be encouraged to work with insureds to act in the wider interest of society.

Insurers must also be ready to seize the opportunities to support the shift away from oil and gas, especially across Europe as major economies struggle to adjust to the impact of the war in Ukraine.

"It will accelerate the big drive to alternative energy sources, such as renewables and in some countries, including the UK, nuclear power. This will require a positive response from insurers."

The need to rethink the approach to ESG issues goes well beyond Europe, says Andrés Amunátegui, Partner – Head of LatAm at DAC Beachcroft in Chile:

"From a Latin American perspective the relationship between these three concepts is not as developed as in Europe and in the United States. Some of the responses have similarities, however, especially building collaboration beyond the usual partners.

"How do we connect with and respond to the challenges facing local communities affected by, say, the heavy rains? It is the first time we have tried to work with local communities and local government to meet these challenges. It has been very exciting to see what a difference this sort of collaboration can make."

SOCIAL UNREST

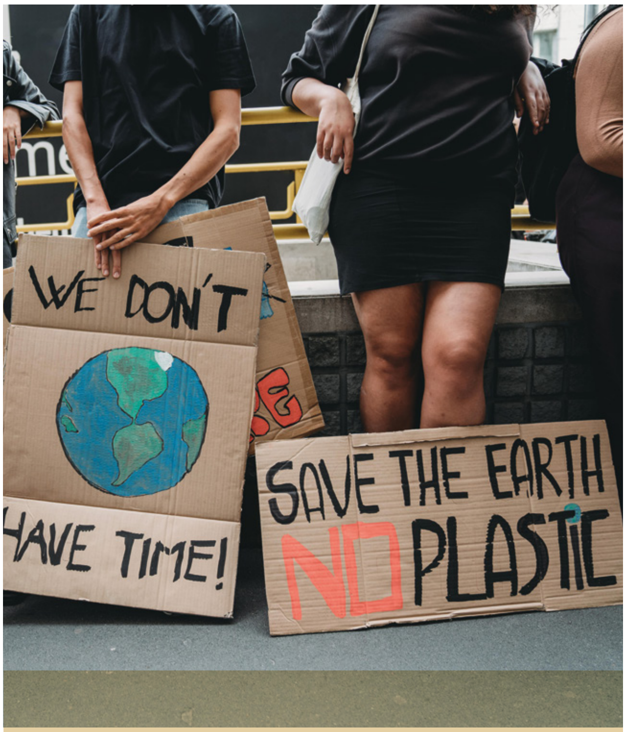
Latin America is a diverse and complex region, mixing stable, developed democracies with others where social unrest is never far below the surface, and this adds to the challenges faced by insurers and their legal partners.

"Here in Chile, for instance, we are currently facing a new social crisis because of the closure of one of the most important mining companies in central Chile as a response to the heavy pollution there over the last fifty years. It creates a dilemma that is very difficult for government to resolve, so we are now facing protests. However, in some parts of Latin America, Guatemala for instance, communities want to be collaborative and avoid violence and conflict.

"If we are going to modernise our infrastructure and move to renewable energy, the solution lies in empowering local communities and delivering them benefits. Renewable energy facilities will have to be built on land owned or claimed by indigenous communities and there has been violent opposition to some projects. Getting co-operation is crucial."

He says building strong relationships with a wider group of organisations is essential if the insurance industry is to avoid getting caught in the traps littered across the region:

"We know about the problems from a professional perspective because we are very close to our insurance clients. We have seen how class actions can become very politicised and influenced by drug cartels and organised crime."



PROTECT DUTY LEGISLATION

The need for the insurance industry to be ready to respond to growing social unrest and terrorist threats is a problem nearer home too, in particular for the UK insurance market with the new protect duty looming ever larger on the horizon.

"The protect duty is another example of the government shifting responsibility onto the private sector but it is more complex than that," says Strachan.

"Even without this legislation, the private sector could still have faced claims. There is a public enquiry in the wake of the Manchester Arena bombing and civil litigation can be anticipated.

"What the new laws do is bring clarity as to where responsibilities lie. It should help the mitigation of risk and prevention. Venues, promoters, security firms and operators will need a clear set of mitigation measures and response plans with systems and protocols in place to protect people. This will have to involve local authorities and the police, especially as it will apply to parks, beaches and many other public spaces."

It could also be a further stimulus to insurance innovation, similar to the need to create policies that help equip our housing stock to be more resilient to climate change.

"Terrorism insurance is traditionally first party focused, with property and business interruption (BI) being the main areas of cover and Pool Re as the government backstop. That has adapted to offer non-damage BI. The question now is whether it will adapt further to cover the new third party liabilities that we expect to see emerge under the protect duty heading.

"There could even be an opportunity to create specialist 'protect duty' policies that offer a range of cover to meet the new risks identified by the legislation for multiple stakeholders," says Strachan.

This would require the sort of collaboration between brokers, insurers, insureds and law firms that is set to become a hallmark of the new ESG era.

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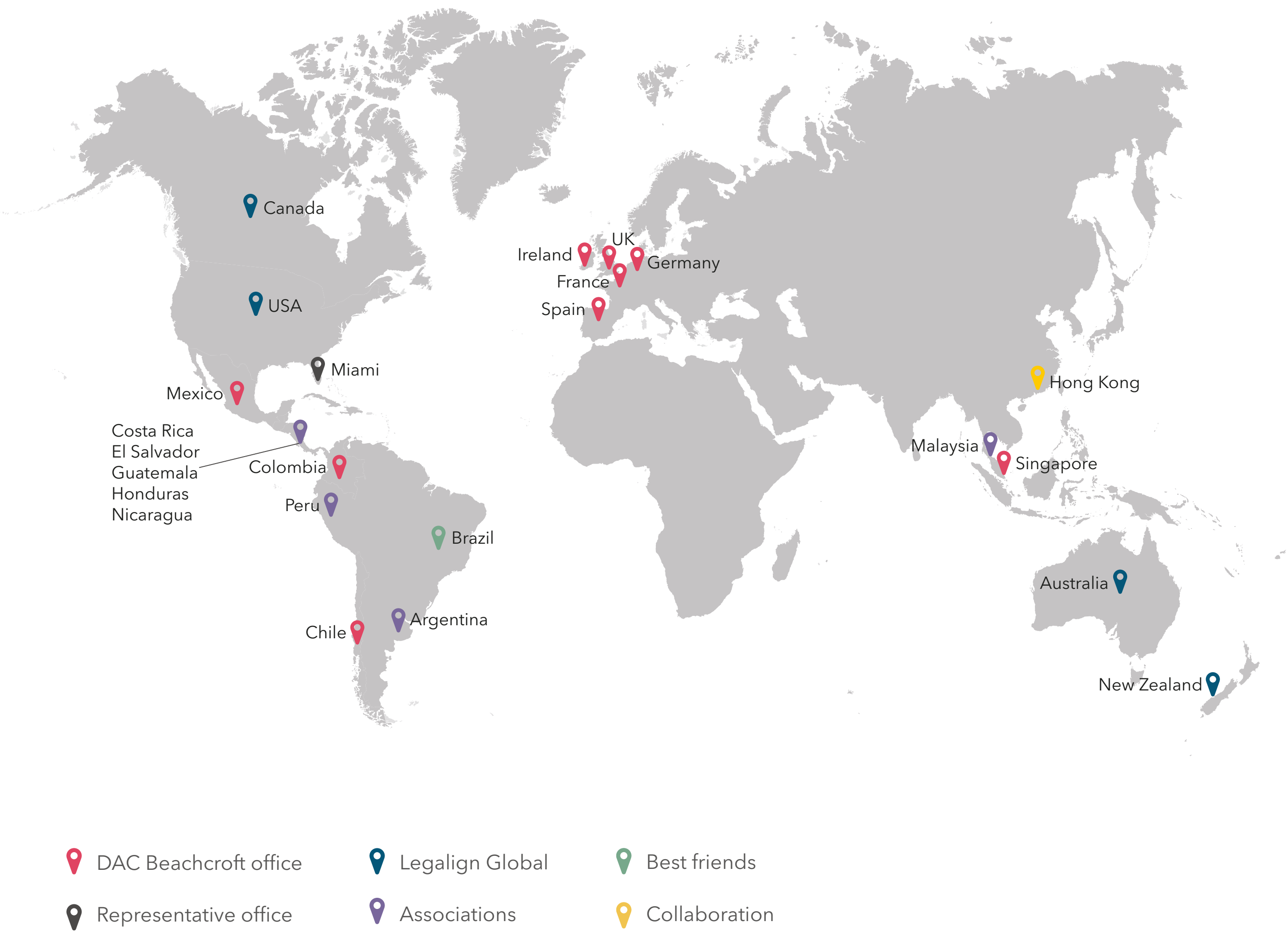
OUR GLOBAL REACH



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