# ESG in claims

## Vision, strategies and decision-making for better outcomes

**Claims transformation**

One of a series of seven insightful and instructive articles that examine a set of interconnected themes and trends that are expected to drive the traditional claims function into a new future of customer-centric, digitally-enabled, value-driven service and efficiency.

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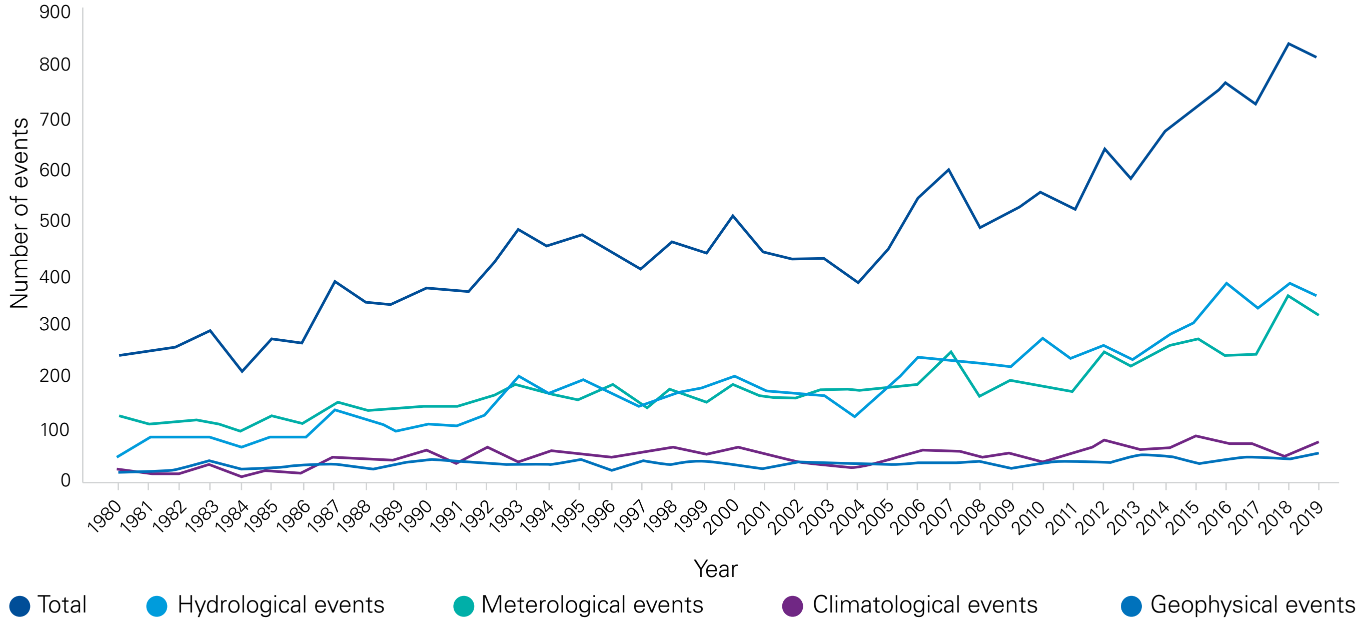
**Given the nature of their business, insurers are in a unique position to connect with a wide range of individuals and businesses to positively influence public behavior concerning today's important social and environmental issues. ESG is one of the seven forces that are transforming the claims function and is explored further in this article.**

Claims teams in particular are well positioned to engage with clients and take on a leading role in the commitment of their businesses to environmental, social and governance (ESG) issues.

While insurers, like all businesses, have a responsibility to implement sustainable practices, and to respond strategically to ongoing social changes and evolving public expectations, a focus on the climate agenda is also good business amid today's increased risk and the destructive impacts of climate change, as the chart indicates.

**Natural catastrophes on the rise — Number of relevant loss events by peril 1980–2019**




Earthquakes, storms, floods and droughts — the number of recorded loss events resulting from natural disasters has been increasing for some years now. Causing overall losses of USD210B, the costliest natural disaster of all time is the Tohoku earthquake, which occurred in Japan on 11 March 2011. In terms of insured losses, the costliest natural disaster to date is Hurricane Katrina, which hit New Orleans in August 2005 and cost insurers a total of USD60.5B (original values).

Source: https://www.munichre.com/en/risks/natural-disasters-losses-are-trending-upwards.html

## The social agenda takes on new global prominence

The social agenda continues to gain prominence worldwide as society speaks out on human rights, equal opportunity and gender and racial equality. Public expectations of businesses are growing accordingly; ethical and inclusive practices are in the spotlight and facing public scrutiny as never before.

Society as a whole has never been more aware of the impact of contemporary life and business practices on society and our environment. Insurers are wisely acknowledging and responding to the importance of embedding ethics and sustainability into their strategies.

Companies can no longer get away with 'greenwashing' — conveying a false impression of ESG progress, and instead need to clearly demonstrate their ESG focus to all stakeholders. The claims function is the 'moment of truth' for clients and ensuring a positive journey and outcome is crucial to reputations and success.

Ultimately, as insurers face greater scrutiny and rising expectations on the ESG front, forward-looking firms are making strategic efforts toward decision making that takes into account today's pressing issues and all that they entail concerning environmental needs, social impacts and potential regulatory requirements.

## Do you know what your suppliers are doing

Building a robust governance structure that aligns decision making with sustainability strategies has become crucial. Global market leaders in every sector, including today's leading insurers, are recognizing the value of this approach and making progress through their actions. Doing so can help facilitate the selection of partners and suppliers sharing the same ethical mindset and give insurers greater confidence across their value chains.

Large organizations increasingly are being held accountable by their clients, stakeholders and the public for the behavior of their suppliers, and insurers are no exception. Reputations can be tarnished in an instant by questionable practices that can come under global scrutiny and severe criticism in today's connected world. Suppliers should possess values which ensure ESG best practice, protect reputations and the bottom line.

Market leaders are pivoting their strategy to include sustainability at their core and how it can shape their value. This includes greater emphasis on addressing and meeting the United Nation's Sustainable Development Goals (UN SDGs). As a result, they are reporting on an increasingly wide range of content and activity, with the volume of shared information growing accordingly for investors, stakeholders and other parties.

For example, a global British consumer goods company now completes a 'materiality assessment' each year to ensure that its strategy is focused in the right areas, continually assessing the changing sustainability landscape and prioritizing key issues impacting the business and its stakeholders. The materiality assessment is helping the business evolve its strategy and tailor its reporting, communication and disclosure as the organization's interests and needs change.

Meanwhile, a major global financial institution has become more transparent about its position and objectives by creating a comprehensive ESG reporting framework, and providing definitions and measurement methodology for key performance metrics in their annual ESG Report, referencing the Sustainability Accounting Standards Board (SASB) and the Global Reporting Initiative (GRI) standards.

## Leading the way on today's ESG agenda

Wider reaching sustainability reporting is likely to become obligatory in the coming years, including the incorporation of the Task Force on Climate-related Financial Disclosures (TCFD) which is now mandatory for large UK companies and financial institutions.[1] Insurers will need to possess the metrics and infrastructure to reliably report progress on key areas, including but not limited to carbon footprint, gender pay gaps and inclusion practices.

Where relevant to the business, going beyond what is required by law will likely increase transparency among stakeholders, enhance communication with clients and the industry, and differentiate insurers as being informed, proactive and forward-looking. The infrastructure required to compile this data takes time to embed, making it vital that insurers focus on the data they need now while preparing to meet future requirements.

There is a risk that some insurers may simply remain focused on minimum targets rather than putting ESG at the heart of their business culture and strategy. Insurers have an opportunity to make real progress, embedding innovative sustainable approaches within the business, empowering staff to embody positive values and communicating their efforts in compelling ways through reporting.

Some leading global firms are already demonstrating what can be done. We are seeing more companies aligning their best practices and reporting frameworks with the UN SDGs and highlighting their ongoing efforts to meet the UN SDGs.

Insurers leading in this category are likely to be paying closer attention to their suppliers, for example, ensuring that they are following best practices on fair treatment and equitable pay for their employees and contract workers. They may also be focusing on responsible consumption and production — ensuring that the outcome of every claim is responsible and minimizes waste as defined by the SDGs.

## A closely aligned supplier network is now crucial

Claims functions are increasingly aware of the need today to limit the carbon footprint of their activities, and this includes giving clients the option of locally sourced services and labor. Having a strong network of local suppliers is becoming increasingly important for insurers hoping to uphold ESG values and meet targets. Suppliers should be encouraged to integrate similar targets into their own businesses, creating continuity and visibility through the value chain.

Recent examples of companies embedding ESG into their supply chain include a British grocery retailer that pledged to remove one billion pieces of plastic from its UK operations. They made it clear to suppliers that packaging will influence which environmentally friendly products are sold in its stores.

A global healthcare company, has announced an ambitious target to ensure all direct suppliers are targeting 100 percent renewable power by 2030. To reach the target, they will work alongside suppliers, sharing key learnings on embedding renewable power throughout its operations.[2] These examples highlight the many ways insurance organizations could challenge themselves to think about all elements of E, S and G.

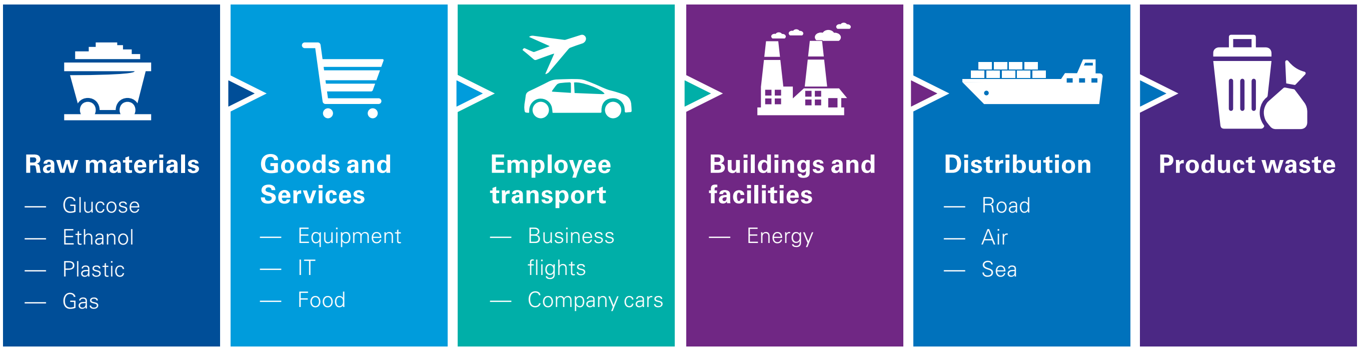
## Understanding the spirit in addition to the letter of coverage

Given the nature of their services, insurers are often the first 'port of call' during times of hardship for clients who are dealing with a loss and need support. Insurers could consider the spirit of a policy and ensure that their clients are fully aware of any caveats and clauses within the policy wording which may impact them in the future during completely unforeseen circumstances like natural disasters. This would support the wider community and positively impact the insurer's reputation. There is also the opportunity to feed into loss prevention services, to limit the potential claim event from occurring in the first place.

[1] https://www.anthesisgroup.com/mandatory-tcfd-climate-risk-reporting/
[2] https://www.novonordisk.com/news-and-media/news-and-ir-materials/news-details.html?id=27497

A global healtchare company strives to reduce $CO_2$ emissions from their activities and value chain as a part of an overall ambition to have zero enviromental impact.

### Tracking carbon emissions at each step of the value chain




Source: White Paper on Climate Change, European Federation of Pharmaceutical Industries and Association, June 2020.

For instance, many policy holders were affected by the Covid-19 pandemic and suffered significant losses, and corresponding claims under their business interruption (BI) policies. In the UK, some insurers accepted liability under 'disease clauses' while others disputed liability, requiring additional clarity from the UK's Financial Conduct Authority (FCA). The court ruled in favor of policyholders regarding coverage for BI losses in the wake of the pandemic, impacting 370,000 policies.[3]

A combination of factors suggest that we are on the cusp of change. Regulators are expecting businesses to do more to support clients experiencing hardship, while the global pandemic and ESG agenda have both increased the focus on sustainable values, ethics and trust. An insurer who focuses on 'doing the right thing' for their clients will likely drive significant benefits and progress for both society and their business.

## Embedding sustainability into your culture

Once the appropriate governance structure is in place to assist in strategy execution, each process within the claims function should be reviewed through a sustainability lens. Market leading insurers will look at the environmental, social and governance impact of each process and identify how they can be improved. A clear set of guidelines will need to be set from the top of the organization and implemented across various functions.

ESG must be embedded in business strategies and form the overall narrative and *purpose* of today's organizations. Every aspect of business operations are in the spotlight today — how employees are treated, supply-chain practices, environmental credentials, responsible use of client data and more. Being a 'purpose-led' organization that strives to have a positive impact on the planet and its people matters today as never before.

An effective way to embed sustainability is to encourage and listen to the views and insights of employees. Today's employees, see employment as a partnership and want a voice in how the business is run. By giving all staff a voice in shaping strategy and policies, insurers can drive progress while ideally limiting attrition and boosting engagement and productivity.

Employees also have a role to play regarding ESG's social aspects. Promoting diversity among the workforce should be high on every business agenda. Claims functions should focus on training or retraining people to provide the skills needed for future employment and advancement, as well as developing employees to contribute increasing value to the business.

## Focus areas to embed ESG

### Suppliers

Ensuring that supplier values and practices align with the insurer's is critical. For example: motor vehicles, replacing damage with second-hand parts where feasible, waste disposal that is environmentally friendly. Property, safeguarding against future damage, energy efficient housing.

### Internal policy

Internal procedures and policies need to ensure that sustainability is at the heart of how the business is run. Policies must be clearly communicated across all functions.

### Learning and development

Insurers should train their people to promote sustainability and work with them to ensure efforts and goals are consistent and incorporated into the workplace culture.

[3] https://www.fca.org.uk/news/press-releases/supreme-court-judgment-business-interruption-insurance-test-case

## Collaboration has become critical to progress

Insurers can also drive progress by working together and sharing best practices. Historically, insurers have pursued a more short-term competitive advantage, but sustainability is an area in which collaboration can make a powerful difference. Market-leading companies across different sectors are already sharing experiences and expertise and working together in new ways to implement smart changes for a better future.

Insurers hold huge amounts of data that can be amalgamated and leveraged to inform public policy and enhance loss prevention. They can continue to work more closely with governments and policymakers to provide new perspectives and insights on risk and modelling, for example, looking at data related to health claims, traffic accidents, weather impacts, travel issues and shipping claims. In this way, insurers can be a real force for good in the fundamental shift required for the world to be truly ESG focused.

### Making a difference — four steps for progress

ESG is complex and informs many different aspects of business. Think about what it means in the claims area by considering these four points that can make a difference:

1. **Define how the claims function feeds into the overarching ESG Strategy for the organization**. Understand how claims can promote ESG practices and the ESG ambition of the insurer and start to take a leading role.
2. **Review current processes through a sustainability lens**. Use ESG criteria to understand what the current ESG impacts are of the claims function and the wider supply chain, to identify areas of concern and opportunities to work more in line with the ESG ambition.
3. **Encourage suppliers to work within the same ESG values**. Promote sustainable practices with suppliers and other relevant parties.
4. **Identify the ESG data which will be required in the future**. Review current data collection and system inputs which will be required in the future for reporting, and can provide insight and value to clients.

Explore our *Claims Transformation* articles series further to learn how the seven forces are affecting the claims function.

If you'd like to discuss how KPMG professional can help your organization with its claims transformation journey, please contact us.

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