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Nudging the world towards sustainability

Insurance as prediction and prevention

One way of understanding insurance is to view it as a safety net – a way to limit the damage and/or losses caused by unexpected, tragic events – a burst geyser, a vehicle breakdown, a debilitating disease, or a natural disaster. In line with this view, the job of insurance companies is to calculate and pool risk. If insurers do their job well, people have a way to sustain their current quality of life, even when the unforeseen happens.

Increasingly, however, insurers have ventured beyond merely calculating the odds of unfortunate events, towards influencing or "fixing" the odds. Driven by enlightened self-interest, and armed with the techniques of the behavioural sciences, insurers now nudge and reward behaviours that make deleterious life events less likely. Whether by tracking our driving habits, financial decisions, grocery lists, or exercise routines, insurers have become masters at aligning our behaviours to our secret aspirations – safer, healthier, more responsible living. In a strange twist of irony, insurers are now more aligned to our interests and wellbeing than medical practitioners. While we traditionally trusted our GP and resentfully assented to insurance, now it would seem that insurers actively try to keep us healthy.

The question is whether insurers can wield their new behavioural powers to address other challenges? If we have unlocked the secrets of individual virtue to sustain personal health, wealth and wellbeing, could we also help humanity as a whole develop the environmental and social habits we so desperately need to address the climate crisis, inequality and human rights abuses?

Sustainable insurance

Enter the idea of "sustainable insurance". More than a decade ago, in 2012, the United Nations (UN) Finance Initiative published its "Principles for Sustainable Insurance". These principles aim not only to understand and protect against risk, but also to prevent and reduce environmental, social and governance risks (so-called "ESG" risks). The then UN Secretary-General, Ban Ki-moon, saw in these principles a roadmap for the insurance industry, "…to promote renewable energy, clean water, food security, sustainable cities and disaster-resilient communities"[1]. These principles are also meant to "catalyse and amplify transformational change" [1]. Much like insurers want their clients to adopt healthy, safe and financially responsible practices, so too do insurers now envision, through their products and services, "…a society in which people are aligned and incentivised to adopt sustainable practices"[1].

It is unfortunate, however, that the principles do not quite match the ambition. The four principles include:

1. embedding ESG issues in the decision-making of insurance businesses;
2. raising awareness, managing risk and developing solutions with clients and business partners;
3. promoting widespread action with governments and regulators; and
4. demonstrating accountability and transparency through regular reporting on these principles to the public.

[1] UNEP FI. 2012. Principles of Sustainable Insurance. Switzerland: UNEP Finance Initiative, p.1 – 2.

Much of the actions recommended alongside these principles boil down to "dialogue" rather than "action", and twelve years after these principles were introduced it is not clear whether the industry has managed to transform itself, much less the practices of insurance clients at large. Even the 2020 Change to Principles for Sustainable Insurance (PSI) ESG "*Guide to Managing environmental, social and governance risks in non-life insurance business*" disappoints by being heavy on consultant-speak ("integrate ESG into strategy", "calculate risk appetite", "allocate roles and responsibilities", "set the tone"), but light on case studies of insurance products contributing to effective societal transformation. It should be noted, however, that this guide includes a comprehensive "heatmap" of ESG risks and possible mitigating actions.

To match the ambition of the PSI, and to test whether the power of behavioural insurance can be applied to the urgent sphere of ESG action, here are two initial recommendations.

Step 1: Moral maturity – getting our motivations right

One reason for the lack of progress in sustainable insurance is its predominantly financial motivation. Sustainable insurance is encouraged on the basis of the increasing recognition that "[s]ome ESG issues [are] potentially *financially material* (e.g. climate change, ecosystem degradation, pollution)"[2] [my emphasis]. Beyond the potential costs of ESG risks, insurers are also enticed into this area by "…the correlation between ESG factors and strong performance of companies across industries"[3].

While the fear of costs and the pull of profit can be a successful driver of innovation in insurance, the flipside of this motivation is that when ESG-based decisions are not financially optimal, profit will trump good sense. An example would be the potential profits to be gained from insuring yet more coal, oil and gas exploration or projects.

To achieve traction, the insurance industry needs a proper motivation. Much like insurers have projected for themselves ideals in different spheres of the life of the insured (exercise, diet, responsible driving, prudent financial planning), so sustainable insurance could sculp a picture of the desirable ESG behaviours of the people and companies that insurance companies insure; collect data on these behaviours; and nudge and reward companies in line with these behaviours. The ultimate motivation is human and corporate flourishing – meaningful or worthwhile life and commerce. A by-product of such life and commerce (and insuring it) is the livelihood that is earned in the process.

Step 2: Practical and effective actions

To have the envisioned transformative effect on society, insurers could:

- over time, work towards eliminating insuring projects or clients that conflict with ESG goals, be that fossil fuel expansion or the violation of human and indigenous rights;
- work towards only investing in companies aligned to ESG goals; and
- nudge individual and corporate clients towards the social and environmental aims they subscribe to.

Beyond recognising responsible driving and regular exercise, insurers could also reward more plant-based diets, the reduction of waste, and the lowering of individual carbon footprints.

On the other hand, corporate clients could equally be nudged towards desirable ESG behaviours by rewarding the use of renewable energies, the elimination of waste, and the promotion of human rights.

The sustainability of insurance

Participating in and promoting ESG behaviours among its clientele is not only a step towards sustaining communities and the planet, but also a way of making the insurance industry itself sustainable. Damage caused by natural disasters has made certain geographical areas uninsurable or unaffordable to insure (meaning a loss of clients), while pay-outs have resulted in massive financial losses for insurance companies. Amid this reality, it would be cynical to stop insuring the possible victims of an environmentally and politically unstable world, while providing cover for behaviours that cause the damage.

The insurance industry wields significant power, and with it the potential to shift mindsets and behaviours – for the benefit of clients, the insurance industry and the greater good of society.

[2] United Nations Environmental Programme. 2020. Managing environmental, social and governance risks in non-life insurance business. Switzerland: UN, p.4 (https://wedocs.unep.org/bitstream/handle/20.500.11822/33632/MESGRNLI.pdf?sequence=1&isAllowed=y).

[3] Ibid, p.4.