The LIAJ comments on Public Consultation on Climate risk supervisory guidance – part four

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<tr><th>Question</th><th>Comment</th></tr>
<tr><td colspan="2">Draft supporting material on macroprudential and group supervisory issues and climate risk</td></tr>
<tr><td>Q1. General comments on the draft climate risk ICP 24 related supporting material</td><td>The Life Insurance Association of Japan (the “LIAJ”) appreciates the opportunity to submit public comments to the International Association of Insurance Supervisors (the “IAIS”) regarding the fourth consultation on climate risk related to the insurance sector.

The supporting material should particularly consider three points: (1) climate risks impact the life insurance and non-life insurance businesses differently; (2) insurers play a role in mitigating climate risks; (3) application of capital add-on to insurers would not be a valid measure to address climate risks.

Firstly, the supporting material discusses how the supervisors capture, monitor and address the effects of climate risks. However, it should take into consideration the premise that climate risks have different effects on life insurance and non-life insurance businesses. The LIAJ hence believes that it would be effective to clarify whether the illustrated measures are intended for life or non-life insurance businesses.

Secondly, the supporting material mainly focus on risks of insurers when addressing climate changes. However, when considering supervisory matters within this topic, it is important to take into account the insurers’ role in contributing to the mitigation of climate risks through the engagement with investee companies.

Thirdly, application of capital add-on to insurers (paragraph 35) would not be a valid measure to address climate risks.
Climate risks materialise over a long time horizon with significant uncertainty in the timing and degree of manifestation, which differ greatly from other traditional risks where capital requirement can be calculated based on historical data. While the LIAJ understands the reason to consider mitigation measures of climate risks where necessary, it would be difficult to determine the consistency between climate risks and traditional risks as they have different time-horizons due to the above climate risk characteristics. For that reason, it is unclear that capital add-on would be the best mitigation measure.
As described in paragraph 71 of “the draft Application Paper on public disclosure and supervisory reporting of climate risk”, there are various issues concerning the quality of climate risk related data and calculation. Even if the add-on capital was to be calculated, the determination of the appropriate level of capital add-on would be difficult.</td></tr>
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	To lightly suggest capital add-on without examining these issues would place an excessive burden on insurers and would damage their capacity to contribute to the mitigation of climate risks through investments. For the reasons above, application of capital add-on to insurers would not be appropriate for the purpose of addressing climate risks. The words "or applying a capital add-on" in paragraph 35 should be deleted or be supported by a conditional statement "only if the add-on capital can accurately be quantified".
Q2. Comments on climate change and financial stability risks	The IAIS states that "insurers could contribute to the generation or amplification of systemic risk induced by climate risk events" in paragraph 4. The word "amplification" should be deleted as it is not supported with sufficient and persuasive explanation, and is misleading.
Q3. Comments on data collection for macroprudential purposes	As to the statement "if climate risk-based indicators are not available, exposure-based proxies, such as investment breakdown by high-carbon intensive sectors or NatCat exposures by peril, could also be used" in paragraph 18, it should be noted that the use of sector-based exposures as a monitoring indicator may overestimate climate risks. Individual insurer's climate risks cannot be measured based solely on the sector because insurers take different measures against climate risks even if they belong to the same sector. Also when monitoring climate-related risks, it would be important to focus not only on the values at a single point in time, but also on the change of value over two points in time. Monitoring values only at a single point in time could overlook an insurer's effort to mitigate the GHG emission during a period and would contribute to the pressure for divestment. Since climate risks need to be captured over a longer time horizon (e.g. 20 to 30 years), transition plans would be useful considering insurers' long-term efforts. Therefore, the LIAJ believes that monitoring indicators need to be determined by individual insurer's exposures with the consideration of transitional and other measures rather than sectoral exposures.
Q6. Comments on supervisory response	Please refer to the LIAJ's comments on Question 1.
Draft Application Paper on public disclosure and supervisory reporting of climate risk	
Q1. General comments draft Application Paper on public disclosure and supervisory reporting of climate risk	The IAIS provides consideration to proportionality and burden on insurers throughout the Application Paper (e.g. paragraphs 8, 19, 32 and 76). Climate-related risks disclosure and reporting to supervisors are still under development, and the level of disclosure varies by jurisdictions or insurers. As it is important to have a long-term view to gradually enhance disclosure of climate-related risks, the LIAJ supports the IAIS' consideration on proportionality and burden on insurers in the Application Paper.

Q14. Comments on section 3.2 Disclosure of scenario analysis results	The LIAJ provided the following comment on the second public consultation on climate risk "Draft Application Paper on climate scenario analysis in the insurance sector": "to avoid imposing undue burden on insurers, supervisors should carefully consider when requiring insurers to conduct scenario analysis for supervisory purposes. They should at least determine whether they need to require additional scenario analysis for supervisory purposes after adequately evaluating if such scenario analysis could be substituted with existing scenario analysis conducted by insurers for disclosure purposes to meet the ISSB and other standards." The second bullet point of paragraph 19 implies that scenario analysis is an analytical method, which imposes reasonable burden on insurers, and the IAIS has taken into consideration the amount of actual operational workload for insurers. In this context, we presume that if supervisors require a separate scenario analysis, which would impose additional burden on insurers even in jurisdictions where it is already required to conduct scenario analysis due to climate-related disclosure standards such as the ISSB standards, the decision to have a new requirement implies that the information disclosed in the general-purpose financial statement does not suffice. Paragraph 28 states recommended indicators to be used when contents of scenario analysis based on existing disclosure standards do not meet the requirement of supervisory objectives. The IAIS should clarify that there is a difference between the scope of scenario analysis required by the supervisors for supervisory purposes and the scope of scenario analysis for the decision-making by key users of general-purpose financial reporting. Such difference stems from the discrepancy between the objectives of conducting scenario analysis. Specifically, paragraph 27 explains the objective of scenario analysis for supervisory purpose as "Rather, they are intended to be used by supervisors from both a micro- and/or macroprudential perspective and by insurers to understand the impacts of climate change on insurers' strategy and the medium- and longer-term risks an insurer faces". This should be modified by inserting the following statement after the first sentence: "Scenario analysis is an analytical method, which pose reasonable burden on insurers. Moreover, some jurisdictions already require scenario analysis to provide information to key users of general-purpose financial reporting in line with climate-related disclosure standards such as the ISSB standards. Notwithstanding these existing disclosures of scenario analysis, the reason why supervisory authorities would still require insurers to conduct additional scenario analysis is for the reason the objective of the additional scenario analysis for supervisory purposes differs from the one used for information disclosure. Supervisors may only require additional scenario analysis for insufficient data."
Q30. Comments on section 6.3 Disclosure constraints	The IAIS implies in paragraph 77 that the ISSB standards could be a base for international disclosure standards for climate risks. However, due consideration needs to be given to use information disclosed in accordance with the ISSB standards for supervisory purposes. For example, as life insurers' assets and liabilities have a long-term nature, their climate-related risks need to be mitigated for the

	medium to long term, accordingly. However, while the disclosure requirement of financial emissions of IFRS S2 is one of the useful indicators to understand the relationship between investment exposure of the institutional investor and the GHG emissions of the investee, it does not adequately capture insurers' climate risks in the medium to long time horizon. Therefore, to understand and capture medium to long term climate risks to which insurers are exposed, it would be appropriate to evaluate both the current exposures and forward-looking information (e.g. transitional plans to mitigate GHG emissions) of the investee.