LES ATELIERS DU FUTUR

Recommendations regarding the Downstream Scope 3 Emissions of Insurers and Reinsurers

(Version 10/2024 adapting our proposal from 03/2024 following various feedback)

Introduction

Insurance and reinsurance companies must adopt an appropriate methodology to measure and track their greenhouse gas (GHG) emissions as part of their decarbonization efforts.

The downstream scope 3 emissions of the insurance and reinsurance sector constitute by far the largest portion of the sector's emissions. Its complexity explains why:

- The GHG Protocol has only addressed the area of investments[1],
- The Partnership for Carbon Accounting Financials (PCAF) proposed a complementary approach in November 2022 for insured emissions only ("Standard on emissions associated with insurance[2]").

We believe these approaches need to be adjusted and complemented, particularly with respect to customer relationships, notably in the area of claims management.

I. Insurance Activities Related to Downstream Scope 3

Savings/retirement insurance provides the customer with an opportunity to appreciate the value of the premiums invested, possibly with annuity or disability guarantees.

Non-life insurance, **health insurance** or **protection insurance** (death, disability, annuity, long term care), offers the insured, whether an individual, professional, or company:

- Compliance with insurance obligations and/or peace of mind through risk transfer, facilitating the ownership and/or use of insured assets and the exercise of insured activities, and
- In the event of a claim, compensation for damages suffered or caused, often accompanied by a service, such as assistance, easing the management of this situation.

[1] https://ghgprotocol.org/corporate-value-chain-scope-3-standard

[2] https://carbonaccountingfinancials.com/files/downloads/pcaf-standard-part-c-insurance-associated-emissions-nov-2022.pdf

Activities, whether internal or external, interacting with the final customer related to these value propositions include:
- Distribution,
- Advisory services,
- Underwriting,
- Policy management,
- Claims management (assistance, expertise, in-kind services, indemnification).

Additionally, the management of assets representing technical provisions and capital is another aspect of activities whose emissions contribute to the downstream scope 3 emissions of the insurer.

From this inventory, it follows that the downstream scope 3 emissions related to the final customer in the insurance sector can be divided into three categories:
- Emissions related to life or non-life insurance **coverage** ("**insured** emissions"), excluding claims management,
- Emissions related to **claims management** ("**indemnified** emissions"),
- Emissions related to **investments** ("**financed** emissions").

II. Classification of Emissions in Relation to the GHG Protocol:

A. Insured Emissions, excluding Claims Management, (downstream scope 3 Client) fall under Category 11 of the GHG Protocol

Considering the principle that the "natural" sphere of impact of a company is characterized by the extent of its economic interest[3], regardless of its ability to influence, we accept the PCAF approach of attributing part of the operational emissions (scopes 1 & 2) of insured assets or activities to the Non Life insurer. This PCAF approach is consistent with the guidelines set by the NZIA.

Since the insurer does not directly finance these activities, it is justified to classify the corresponding emissions in Category 11 of the GHG Protocol, titled "Use of Sold Products."

In line with the GHG Protocol's requirements, the attribution factor to the insurer for these emissions can be established through any available data method. The proxy proposed by PCAF—weight of the insurance premium in the total operating budget of the asset or activity—seems appropriate.

[3] https://lesateliersdufutur.org/wp-content/uploads/2024/09/ADF-Sphere-impact-VF.pdf

This attribution factor (specific to each line of activity/insurance-reinsurance segment) should be applied to the scope 1&2 emissions of the client, the asset, or activity insured **for the relevant insurance period** (corresponding to the premiums acquired during the period).

Ongoing work to define these attribution factors across all activity lines (individuals, professionals, agricultural, corporate, and all insurance branches) should continue.

Regarding life or health insurance, considering the emissions of the insured client does not seem appropriate for the evaluation of downstream scope 3 emissions of the insurer.

B. **Indemnified Emissions** (downstream scope 3 Client) fall under Category 11 of the GHG Protocol

The PCAF draft standard does not address downstream scope 3 emissions related to claims indemnification.

In the case of life insurance, savings, and retirement, these emissions are clearly minor compared to the financed emissions.

On the other hand, those associated with non-life claims management appear to be significant[4], and the insurer can play a crucial role in the choice of assistance, repair, or replacement solutions. **The failure to account for indemnified emissions presents a high risk of greenwashing for the sector.**

For example, insurers can influence the emissions outcome through:

- The selection of electric replacement vehicles in the case of an accident or breakdown,
- Offering reused parts for automobile repairs,
- Proposing recycled materials for small property repairs,
- Proposing repairs rather than replacements for damaged equipment,
- Financing more energy-efficient equipment, such as a heat pump, instead of replacing an irreparable boiler,
- Providing an additional indemnity to purchase an electric vehicle in the event of a total loss of a vehicle,
- Choosing repairers or service providers based on their environmental impact.

[4] Cf: https://protectorinsurance.co.uk/getfile.php/137680-1710351826/Documents/Investor%20Relation/Annual%20Reports/ENG/2023%20Annual%20Report.pdf

The insured's GHG emissions can thus be significantly reduced after a claim thanks to the Non-Life insurer's intervention. Some insurers have introduced specific indemnity clauses, called "green clauses."

Therefore, we recommend that Non-Life insurers fully include the emissions related to claims indemnification in their downstream scope 3 emissions, at least for the damages suffered by the insured.

The GHG Protocol establishes a principle of coherence between the timing of emissions and the timing of the company's margins. For example:

- The automobile manufacturer is attributed the **total emissions related to the vehicle's use over its entire lifespan at the time of sale**,
- The bank financing the vehicle inherits a share of the vehicle's **annual emissions**, weighted by the share of the loan in the vehicle's total value.

This principle implies that the calculation of indemnified emissions should consider for each **fiscal year,** the claims assigned to it, based on **when they occur.**

In the case of **property damage claims,** this calculation should include:

- Emissions related, if applicable, to **assistance or in-kind services** provided during the claim (scope 3 of the client),
- Emissions related, if applicable, to the **repair of the damaged assets** (scope 3 of the client),
- Emissions related to the **use of the replaced goods over their residual lifetime** (scope 1&2 of the client), adjusted with an attribution factor (value, weight…).
    - Example 1: **Replacement of a total loss vehicle**: emissions related to its residual use (20 years for a new vehicle, 10 years for a used vehicle),
    - Example 2: Vehicle repair: proportion of the vehicle's emissions related to the **repair part** (e.g., (value of the part / value of the vehicle) x emissions of the vehicle related to its expected usage).

In the case of a **business interruption claim**, the decrease in the client's activity logically leads to a reduction in its emissions across all scopes. However, the insurer's intervention has a dual purpose:

- In the short term, to compensate for the lost income needed to cover fixed costs and regular results. **The insurer should therefore be attributed the emissions related to this share of fixed costs.**
- In the event of a major claim, to prevent the business's failure in the medium term. This circumstance is complex to assess because the failure scenario depends on several factors, including competitive pressure and the

company's equity. This complexity justifies not accounting for future emissions related to such survival.

A lack of data for accurately calculating these emissions may be argued.

In this context, insurers may choose between an "in concreto" approach based on their indemnification activity or a flat-rate approach based on:

- The number of claims by type and severity,
- Carbon intensity factors related to the nature of the claims,
- These factors, in turn, based on parameters generally accepted by national agencies in charge of decarbonization or derived from studies conducted by insurance federations.

Since no financing is provided by the insurer—the indemnity is never reimbursed by the beneficiary—this area also justifies classifying the corresponding emissions under Category 11 of the GHG Protocol, "Use of Sold Products."

C. **Financed Emissions** (downstream scope 3 Investments) fall under Category 15 of the GHG Protocol.

This follows directly from the definition of Category 15 in the GHG Protocol standard[5].

In the case of life insurance, savings, and retirement, these emissions represent an essential part of the insurer's downstream scope 3. Although the assets representing provisions are a source of financial products and asset managers are, from a legal perspective, service providers to the insurer, it appears that these emissions fall under downstream scope 3 rather than upstream.

Regarding non-life insurance, the volume of provisions and therefore assets is lower than in life insurance, but still at a level justifying the consideration of the associated emissions.

Finally, it seems desirable, for the sake of transparency and comparability, that insured, indemnified, and financed emissions be presented separately, on one hand, and in consolidated form at the insurance company level, on the other.

[5] https://ghgprotocol.org/corporate-value-chain-scope-3-standard

III. Line of Business to Prioritize for Indemnified Emissions

For completeness, all insurance branches should, in principle, be covered by the insurer's downstream scope 3 approach. However, given the complexity of the indemnified emissions issue, prioritizing based on their importance and on the insurer's ability to influence seems proportionate and desirable.

The branches to prioritize for assessing these indemnified emissions are as follows:

- Motor own damages,
- Assistance,
- Damage to private or professional property,
- Business interruption insurance.

This should allow for the exclusion from the tracking of indemnified emissions, at least initially:

- Savings and retirement,
- Protection, health insurance,
- Liability insurance,
- Crop insurance.

The insurers should justify their choices of inclusion or exclusion of segments based on these principles.

IV. The Downstream Scope 3 of Reinsurance Follows That of Insurance Regarding Insured or Indemnified Emissions

According to the principle that the "natural" sphere of impact of a company is defined by the size of its economic interest, the reinsurer's role is similar to that of the insurer, both in terms of risk coverage and claims management.

The attribution factor used should take into account the conditions of reinsurance, such as quota share, excess of loss, full reinsurance, aggregate, etc. By analogy with the financial sector, it should be based on the reinsurer's share of the risk, gross of retrocession. The ratio between the ceded premium and the insurer's turnover seems to be a good proxy in this regard.

It is also relevant to classify the downstream scope 3 ("final customer") of reinsurance under Category 11 of the GHG Protocol as well.