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Insuring the Climate Transition A view from risk customers and solution providers on what works and what needs to be improved



Foreword	01
Executive summary	03
Section 1: The role of insurance in the transition	
and key sector challenges	07
Section 2: Hurdles to risk solutions for hard-to-abate industries	13
Section 3: Key recommendations to turn transition challenges	
into opportunities	18
Glossary	26
Endnotes	27
Contacts and Authors	28

Foreword

Climate change is happening faster than anticipated.¹ To turn the tide, the world needs a well-planned transition to a low-carbon, sustainable global economy. The insurance and wider risk management sector stands at a pivotal point, with numerous opportunities to help businesses shift towards renewable energy sources and low carbon business models.

As climate change increases the severity and frequency of extreme weather events, the need for proactive approaches to risk management is also growing. In 2023 the global economic losses from natural disasters totalled US\$380 billion, of which only US\$118 billion was insured.² The impacts beyond the economic losses are far reaching and include human health impacts, business interruption, supply chain failures, and regulatory/ legislative changes. As the world endeavours towards a more sustainable future, the insurance industry's role in helping the net zero transition ('the transition') becomes increasingly significant.

Bringing together the expertise of Deloitte and Aon, we explore the path for insurers and their customers to foster a deeper understanding of the risks at play to drive scalable and efficient solutions. In the spirit of discovering these evolving (re)insurance needs, we interviewed 30 experts spanning EMEA, North America and APAC regions. We gathered perspectives and experiences from insurers, brokers and their customers in hard-to-abate sectors on five key themes: (1) climate transition market trends, (2) challenges specific to hard-to-abate sectors, (3) potential solutions to the challenges raised and relevant examples of de-risking innovation, (4) the role of risk (transfer) solutions to mobilise the transition and, (5) the role of wider insurance value chain participants.

At the time of writing this report, the direction and shape of the climate transition remains unclear. Deloitte's recent research has also revealed how this unprecedented challenge could ultimately require a US\$200 trillion global investment by 2050.³ With the growing costs of climate-related disasters impacting communities around the world, action is needed now to limit emissions and improve disaster preparedness. Businesses will continue to evolve and adapt to the climate transition and the ways in which insurance market participants respond will vary.

There is a critical role for commercial risk transfer solutions – the transfer of exposure to potential loss from adverse outcomes to another party – in de-risking projects to accelerate the transition. Moving away from traditional product-led approaches to holistically addressing climate risks and opportunities will be key. While this report does not include insurance coverage gaps (i.e. certain activities of hard-to-abate sectors that insurers will not be able to cover at the moment), we recognise this still requires attention and it is necessary for businesses to address in their own transition. Practical examples and case studies in this report highlight the work insurers, reinsurers and brokers are already leading to help mobilise financing for transition projects, unlock capital for innovation and develop optimal risk management solutions for the transition. We expect the next few years to be shaped by how effective and deep the collaboration is between insurance market participants, private businesses, policymakers and public sector entities to confront an issue of shared global importance, one that is simply too big and too complex to be addressed by individual participants.

We would like to thank all those who took part in our research and interviews. We look forward to discussing our findings with you.



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Liz Henderson Executive Managing Director Global Head of Climate Risk Advisory *Aon*

Executive summary

Different sectors of the economy are transitioning at different speeds and from different starting points. Yet, climate change is an interconnected, systemic issue requiring integrated solutions across geographies, the public and third sectors, and private businesses. As climate change fuels the severity and frequency of extreme weather events, the need for proactive approaches to risk management is growing. Our report consists of three sections. Section one analyses the role of insurance and the challenges the sector faces in helping businesses manage both new and existing transition risks. The section also presents four challenges our interviewees believe are hindering risk solutions to effectively support the transition. Section two highlights why the pace of transition in hard-to-abate sectors is slower and recognises, through case studies and practical examples, the barriers and opportunities for risk (transfer) solutions. Section three sets out five recommendations that can help increase the pace of transition and identifies key participants that need to be involved in delivering these actions.

Four key challenges that are impeding the availability and effectiveness of risk (transfer) solutions in facilitating the transition are:



Insurance is an afterthought for transition projects.

Relative to project design and financing decisions, insurance coverage is often assumed or seen as 'to be sorted later.'



Insurance is sometimes mismatched to the longer-term needs of a transition.

While recognising the existence of multi-year insurance policies in areas such as construction, insurance renewals and policy terms for many other risks still operate on an annual cycle, often mismatched with the needs of a longer-term transition.



Insurers are largely product-led instead of solution-oriented in their approach to help with the transition.

Insurers typically offer a traditional product-led approach to supporting businesses with their transition. However, the transition will present businesses with novel risks as the activities and sectors in which they operate evolve over time. Product and functional silos within insurers can inhibit the multidisciplinary and multifunctional approach required for developing innovative risk transfer solutions.



Climate transition commitments from international reinsurers are often misaligned with those from insurers in emerging markets.

Climate goals and ambitions of international reinsurers in developed markets are sometimes mismatched to the local realities of insurers operating in these emerging markets, who face different transition challenges. This can limit the efficiency of the global insurance market in accelerating the transition to a low-carbon world.

Taking the challenges on the left and those specific to hard-to-abate sectors into account, we present five recommendations to help increase the pace of the transition.

Recommendation

Consider project insurance at project inception phase.

- Decarbonisation projects are large and complex, involving a range of technical inputs and multiple development timelines. Given the importance of insurance in attracting finance, a concerted effort by participants along the project life cycle to consider insurance and risk management early on is clearly needed.
- As a front-to-back discussion is needed, and early engagement between financiers, developers, engineers and designers with their brokers and risk management partners is key.

Develop and communicate transition plans early to ensure that risk capital remains available and adequate for evolving business operations.

- (Re)insurers, brokers and businesses should all be setting out transition plans, whether or not they are made public, and understand the dependencies that exist between each other's plans. This should include discussion of any risk (transfer) solutions that may need to be created to match future risk profiles.
- For the insured, consider how you communicate and discuss your transition plans with brokers and insurers to ensure that the risk (transfer) solutions you require for future operations are well understood.

3

Realign time horizons for some insurance products from a transactional annual renewal cycle towards a multi-year, multistakeholder partnership approach that incentivises innovation and 'patient capital'.

- The insurance industry should consider longer policy terms than the standard annual renewal cycle in certain instances recognising the existence of multi-year policies in some areas (e.g. major construction projects). The ability to provide stable insurance coverage over long periods can free up capital flows and incentivise investment in clean technologies otherwise not investable at scale.
- Insurance industry associations at regional and national levels should collaborate more freely
 with other participants of a transition project's lifecycle in pre-commercial phases to discuss risk
 (transfer) solutions. This will enable learning and experimenting opportunities that in turn will
 facilitate the pooling of risk and/or the development of new risk solutions that are not dependent
 on pre-existing loss data.

For whom

- Businesses
- Financiers
- (Re)insurers
- Brokers
- Businesses
- (Re)insurers
- Brokers

- Businesses
- Financiers
- (Re)insurers
- Brokers

Recommendation

Appreciate that not all risk management and risk (transfer) solutions to transition barriers will be product-based.

- Insurance products may not necessarily be the solution to all questions around the de-risking of transition projects.
- Insurers and brokers can help close coverage gaps through their risk engineering and risk consulting capabilities. This can also help insured parties to better understand the interventions that help secure coverage, which may not be available, and make a stronger case for the underwriter looking at the risk.
- Brokers can play an important role as the main conduit through which businesses buy insurance. Brokers could potentially be asked to perform due diligence on their clients to make sure that the business they are placing complies with the criteria set out by insurers. Innovation and front-to-back thinking will not happen without adjustments to incentives and compensation.

Go 'back to basics' and embrace uncertainty concerning future liabilities as an advantage for underwriting.

- While the lack of relevant historical data could make quantification of climate risks challenging and prohibits the validation of predictive models, the insurance industry has a long history of dealing with new risks. This legacy of adaptability will be useful in dealing with climate-related risks.
- Exploring and utilising a wider range of data sources, including 'adjacent' risk data, can help insurers and businesses develop a more customised view of risk. The use of multiple data sets and models can also help solve challenges around unpredictability as well as differences in assumptions relevant to different geographical regions.

• (Re)insurers

For whom

Brokers

- (Re)insurers
- Brokers

- We would like to thank the following organisations for sharing their views with us.
- Advario
- a.s.r
- AXA XL
- Climate Wise
- Fidelis Insurance Group
- · Heidelberg Materials
- Kita Earth
- Liberty Mutual
- LyondellBasell Industries
- Maersk

- Momentum Metropolitan Holding
- Munich Re
- OMV
- Philips
- Royal BAM Group
- Santam
- Signify
- Swiss Re
- Tata Steel
- United Nations Environment Programme Finance Initiative

Section 1: The role of insurance in the transition and key sector challenges

The transition will require businesses to manage both new and existing risks. Known risks are, of course, well understood by risk managers and their associated risk transfer needs typically well catered for by the global insurance market. In addition, businesses can also create risk management and selfinsurance solutions of their own where risks are well understood. However, the transition will also present businesses with novel risks, as the activities and sectors in which they operate evolve over time. However, more can be done to raise awareness of climate challenges and the opportunities to scale climate action across the global business community. For example, a recent Global Risk Management Survey by Aon (based on approximately 2,800 respondents across 16 industries) found that engagement with the threat presented by climate change and the need to transition was somewhat muted.⁴ In their 2023 study, climate change was neither explicitly cited as a current, nor future top 10 risk by the businesses surveyed. It seems that climate change risk is underestimated by businesses that are yet to appreciate the full impact and associated risks of climate inaction. However, it can also be observed that climate change influences nearly every top 10 risk identified in the survey, either directly or indirectly.

A key transition challenge is that the financial impact of transition planning – insurance-related or otherwise – is currently unassessed. While this challenge is outside the scope of this report, it is important to recognise this as an overarching hurdle for any industry.

Multiple participants will be involved in the insurance value chain of a transition project (see Figure 2). Each actor has its own role to play, and leading firms can turn transition challenges into tangible opportunities. This includes advancing the available range of risk (transfer) solutions in the market, to ensure they are both accessible and affordable for businesses.



Figure 1. Top 10 risks identified by business leaders

Source: Aon Global Risk Management 2023 Survey.



Figure 2. Key insurance value chain participants in a transition project

Source: Deloitte and Aon analysis of key participants involved in the transition insurance value chain.

For (re)insurers, their role as a trusted risk adviser in the transition will help businesses understand risk, assess viable options to mitigate identified risks and provide access to risk transfer capital where other risk mitigation options are limited. The potential means of involvement by insurers and reinsurers across the lifecycle of a transition project is illustrated in Figure 3.

Figure 3. Example areas of involvement by (re)insurers across the lifecycle of a transition project

Project phases	1. Conceptualisation	2. Feasibility assessment	3. Pre- engineering design	4. Engineering design	5. Execution	6. Operation
Example milestones	Project site decided and approved	Design principles and assumptions approved	Technology selection approved	Final investment decision made	Procurement and project construction	
Potential touchpoints with (re) insurers and risk engineering teams and associated benefits	1 Identification of site-specific physical climate risks	2 Identification of technology risks, due diligence and integration into the local environment (regulations, supply chain, infrastructure, third- party risks etc.)	3 Managing physical climate risks to enhance insurability (e.g. having contingency plans against the risks and real-time risk monitoring)	4 → 77 Final assessment of construction and operational risks, and other risk management measures	raditional touch point	of (re)insurers

Source: The Geneva Association, Bringing Climate Tech to Market, April 2024.

Our interviews identified four challenges that may hinder risk (transfer) solutions in facilitating the transition:

- insurance policy negotiation is predominantly an annual activity, mismatched with the needs of a longer-term transition.
- 2. project insurance is an afterthought relative to project design and financing decisions.
- 3. product-led thinking and silos in insurers impede innovation and scaling of risk management and transfer solutions.
- 4. misalignment of climate transition policies and commitments between international reinsurers and emerging market insurers challenge the efficiency of solving a global climate problem.

Each of these challenges is discussed in more detail below.

1. Insurance policy negotiation for certain risks is an annual activity, mismatched with the needs of longer-term transition investments

Insurance runs on annual policy cycles for certain risks, which are not immediately conducive to the longer-term view required for transition planning. Unless this challenge is addressed, (re)insurers and brokers could lose the opportunity to play a much fuller role across the risk value chain, and become excluded from key strategic discussions that businesses are having concerning the transition.

In this scenario, insurers also run the risk of not being seen as the go-to risk partner for businesses carrying out their transition plans. Indeed, many could turn to other providers, create their own novel risk solutions, set up and/or utilise their captives ('self-insure') or work with other partners.



My bank talks about how they can assist us in the transition, but my insurer hasn't asked about our transition plans.

Risk Manager at an international business

2. Project insurance is an afterthought relative to project design and financing decisions

Insurance is too often considered a secondary priority, after investment has been secured. In reality, though, early engagement with the (re)insurance sector, at the project conceptualisation phase, would help optimise risk management approaches and limit the cost of equity, debt or other capital being sought.

This is especially true in the case of breakthrough technologies like green hydrogen and biofuels, where higher project costs are at least in part driven by the associated risks. This can deter the mobilisation of capital at scale for important projects even though their commercialisation is critical for abatement.

Finding risk solutions for new or emerging risks also takes time. Collaboration with risk engineers and risk consultants at the outset allows firms to bring valuable expertise to the table earlier in the process and reduce – or even eliminate – project risks before reaching project finance stage. This improves project 'bankability' and helps to attract and diversify sources of capital.



Interview insights

The finance problem is not solved yet. Insurance comes next.

Director of new energy at a major steel producer

The role of insurance in the climate transition is secondary. Financing is primarily driving the transition.

Sustainability Manager at a Dutch insurer

3. Product-led thinking and silos in insurers impede innovation and scaling of risk management and transfer solutions

Many insurance firms are product-led and organised in silos that make it difficult for different parts of the company to work together. This is especially challenging for product innovation relating to climate transition, which often requires multiple disciplines coming together to develop novel underwriting and risk transfer solutions.

Moreover, insurers increasingly rely on data from multiple external sources to develop products, especially for emerging technologies with a limited track record.

Greater collaboration with third-party technology validators (e.g. professional industry associations, standards development bodies, engineering firms, academic institutions and non-profits), financiers and project developers themselves, would be helpful in building confidence around performance expectations and solving insurability challenges for emerging technologies.



Interview insights

The industry thinks too much about product lines. When climate change will touch each of our underwriting lines, and green technologies are developing at pace, there is a significant need to be very collaborative within our own organisation and also with external partners in terms of how we understand future risk profiles.

Head of Energy Transition at a large UK insurer

4. Misalignment of climate transition policies and commitments between international reinsurers and emerging market insurers challenge the efficiency of solving a global climate problem.

Currently, low-carbon transition in emerging markets relies heavily on public sources of finance, but private sector finance is needed for the world to be on track to meet net zero targets. For instance, the International Energy Agency (IEA) notes that by 2030, annual capital spending on clean energy in these economies needs to expand by more than seven times, to above US\$1 trillion.⁵

Insurance is a critical piece of the mosaic of solutions being considered to help increase private finance for low-carbon transition in emerging markets. This includes utilising reinsurance capital to scale blended finance vehicles and to increase multilateral support for green projects.⁶

When insurers in different regions need insurance from international reinsurers, they may also find that the climate policies and commitments of reinsurers are not aligned, presenting challenging targets. Such misalignment presents a significant challenge to the efficiency of the global insurance market in its mission to help solve the global problem of climate change.



Interview insights

As an insurer in a developing country, there is a fine balance of supporting the transition which will take longer for us and having to rely on global reinsurers who have made sustainability commitments themselves and request us to contribute to these challenging targets.

A developing market insurer

Collaboration with financial institutions and engagement with government bodies are crucial to facilitate the transition.

Director at a European insurer

Recognising the role of governments

While this report does not explicitly discuss the role of governments and policy makers in insuring the climate transition, we recognise that government is, in many ways the 'insurer of last resort' stepping in to prevent or manage instances of market failure.

Insurers and reinsurers face risks of worsening effects of global climate change. Climate change may present new challenges to insurers with severity of losses that the industry has not previously seen resulting in rising premiums and/or insurers having to reduces risks to their own financial solvency. There is a need for concerted efforts by insurers, regulators, governments and risk solution buyers at large to ensure that the appropriate balance is struck for the affordability and availability of climate-related risk (transfer) solutions. Broader measures, often not under direct control of the insurance industry, will need to be aligned with insurers' continuous assessments of underlying risks to seek risk solutions that is affordable and readily available to businesses.

Governments have a key role to play, often looking to the insurance industry to help them understand their own risk exposures, as well as the role that private capital can play in efficiently transferring these risks. Government intervention at local and national levels can help in areas such as:

- establishing legislation and regulations to incentivise investment in renewable energy and other clean technology areas. For example, the Inflation Reduction Act (IRA) in the US has seen US\$110 billion invested into clean energy projects since August 2022, with 60 per cent stemming from foreign companies⁷
- increasing climate adaptation through a combination of public and private financing for transition projects, as well as laying out guidelines within which financial institutions can more easily cooperate and accelerate climate adaptation
- supporting green infrastructure projects by providing state-backed reinsurance to alleviate cross-border investment risk where the private sector has a limited risk appetite
- creating or enhancing risk pools that explicitly focus on climate risk and could help in post-disaster relief (e.g. funding the sustainable restoration of damaged infrastructure).

Section 2: Hurdles for risk solutions for hard-to-abate sectors

One of the core climate action challenges we face is how best to transition critical energy intensive economic sectors like heavy industry and long-distance transport, which between them account for approximately thirty per cent of global greenhouse gas (GHG) emissions.⁸ These sectors are often referred to as 'hard-to-abate' because they have few clear, viable, low-emission alternatives to the fossil fuels they currently rely on.

Deloitte's *Pathways to Decarbonisation* series presented the challenges hard-to-abate sectors face in this regard providing insights into the viable solutions available to businesses in these sectors (see Figure 4).⁹ The global economy, and wider society, depend on these material – and energy-consumptive industries. And so, by helping them to transition with timely and affordable risk (transfer) solutions that support climate action, the insurance industry can assist in helping the global community avoid some of the worst impacts of climate change.

As a result of these challenges, the pace of transition in hard-toabate sectors is slower, and the problem can be aggravated further by regional or sectoral differences as well as interdependencies between them. While this report does not express a view on the state of the transition across these hard-to-abate sectors, we nonetheless recognise through case studies and practical examples the barriers faced, as well as the potential opportunities for risk (transfer) solutions, as part of the sustainable business transformation to net zero.

Figure 4. Key transition hurdles faced in selected hard-to-abate sectors

Select hard-to-abate sector	Key transition hurdles
Heavy road transport	 Supply chain limitations and complex value chains make it substantially more difficult to determine CO₂ emissions on a comparable basis. Limited financing and insufficient regulatory incentives. Significant renewable electricity capacity required for alternative technologies to be developed. Limitations to infrastructure, such as charging and fuelling infrastructure for a switch to battery and hydrogen technologies, and lack of standardisation needed to cover entire road networks.
Steel	 Varying maturity of decarbonisation technologies and shortage of relevant skills. Shortage and cost of green hydrogen and renewable electricity. Variable demand from end-consumer markets. Limited regulatory framework to level the playing field, with a lack of clear certification standards. High financing and capital expenditures. Scarcity of raw materials.
Chemicals	 Low supply of green electricity and associated risk of insufficient and non-cost-competitive supply. Uneven playing field in carbon leakage management. Variable demand from end-consumers. Lack of transparency in carbon measurement and reporting. Slow technology development and implementation.

Source: Deloitte Pathways to Decarbonisation series

Case studies and practical examples

The case studies presented in this section illustrate the practical barriers and potential opportunities for businesses, and the role of insurance and brokers in bringing together a shared transition effort. It is evident from these case studies that impacts are felt across all dimensions of a business' value chain.

Businesses, financiers, (re)insurers and brokers are experimenting and learning to understand transition risks and create new solutions and best practices despite the challenges mentioned previously. Indeed, a broad perspective, collaborative attitude and a willingness to engage in pre-competitive experimental learning opportunities are all potential critical success factors to innovate around risk (transfer) solutions that are more easily available and affordable.

ИЦ

Case study 1: Establishing a hydrogen facility

The problem: Hydrogen is increasingly regarded as a legitimate alternative energy carrier to fossil fuels and, on that basis, is set to play a vital role in the energy transition across multiple industries. However, developers and their financial backers can find it challenging to secure adequate insurance coverage across all elements of the project life cycle. The ability to access insurance and de-risk projects is critical to unlocking and accelerating the development of a hydrogen economy and to mobilise capital quickly. Hence, to grasp the opportunity that hydrogen presents as an eco-friendly alternative to fossil fuels, it is vital that the industry both understands and articulates its risk transfer challenges through all phases of hydrogen projects.

The outcome/solution: In one recent case study, Zurich Insurance Group (Zurich) and Aon launched a pioneering clean energy insurance facility, providing comprehensive coverage for blue and green hydrogen projects with capital expenditures of up to US\$250 million.¹⁰ Both parties conducted extensive research and engaged with customers to gain insights about the specific needs and challenges of developing these projects. The resulting multi-line clean energy insurance facility offers comprehensive coverage through a new, single integrated policy, with cover that encompasses construction, delayed start-ups, operational risks, business interruption, marine cargo limits and third-party liabilities. It also includes coverage for CCUS technologies, providing customers with a complete suite of solutions across the entire value chain of hydrogen production.

Blue hydrogen: The carbon-neutral process of extracting hydrogen from natural gas mixed with very hot steam and a catalyst. A chemical reaction occurs creating hydrogen and carbon monoxide. Water is added to the mixture turning the carbon monoxide into carbon dioxide (CO_2) and more hydrogen. The CO_2 emissions are captured and stored underground.

Green hydrogen: The production of hydrogen through the electrolysis of water using renewable energy resulting in low-carbon emissions and no requirement for carbon capture facilities.



Case study 2:

Technology performance guarantees renewable energy and battery energy storage systems (BESS)

The problem: While there is an urgent need to accelerate capital flows to support the low-carbon transition, including the further development of renewable energy and other green technologies, directing the required capital towards these projects can be challenging. For example, the relatively limited availability of data concerning the energy producing potential of different green technologies makes it more difficult to demonstrate the financial viability of projects. This can be a particular issue in BESS technologies that are vital for the development of the sustainable energy grids of the future, and where renewable energy and battery performance are key factors. Currently, battery manufacturers will typically cover customer warranties, creating significant long-term liabilities on their balance sheets, potentially hindering their ability to obtain additional future investment.

The outcome/solution: Technology performance guarantees can help early-stage businesses secure debt financing by insuring against a shortfall in renewable energy production caused by an underperforming technology. This, in turn, helps smooth cash-flow volatility for projects, helping lenders feel more confident that debt payments will be made on time and on target.¹¹



Case Study 3: Addressing the challenges of advancing carbon capture and storage (CCS)

The problem: CCS is a key technology that can reduce global emissions and help businesses reach their net zero goals. Demand for CCS projects - which remove carbon from the atmosphere through a process of capturing, transporting and permanently sequestering CO₂ below ground – is growing.¹² Many governments are investing significantly in CCS as part of their transition strategies with the UK for example having pledged to invest £20 billion in early deployment of the technology and the US pledging US\$12 billion over the next five years.¹³ However, there are unique risks associated with CCS projects, particularly during the operational stage of the project lifecycle, with carbon dioxide leakage a critical risk area. Additionally, some governments, such as Japan, are looking to invest in overseas projects through which they can transport domestically produced carbon to be stored in foreign locations. This brings with it additional project risks associated with different regulatory regimes as materials are traded across international markets.

The outcome/solution: Specialist products that align with a project's local regulatory regime, contractual obligations and financing requirements can help to solve the challenges associated with a lack of standardised regulatory policies.¹⁴ In this case study, Aon's CCS product provides comprehensive cover across physical damage, well control, loss of revenue and liabilities for both offshore and onshore projects. It also covers the unique risks associated with CCS projects once operational, such as reservoir integrity and indemnity for lost tax or carbon credits owing to carbon dioxide leakage during transport or storage.





Case study 4:

Mapping sector decarbonisation pathways and interdependencies

The problem: To have a credible pathway to 1.5°C, carbon intense sectors need to map out their decarbonisation pathways over the short, medium and long term.¹⁵ While this is often done at the company and sector level, dependencies with other sectors' transition pathways, including technology and finance requirements, are often poorly understood.

The outcome/solution: To better understand the key dependencies between sectors, ten carbon intensive sectors mapped out key technology, policy and financial barriers, including insurance requirements. These highlighted the dependencies, alignment with key 1.5°C milestone, and the financing requirements to enable the decarbonisation roadmap to be delivered. For example, the future of energy generation mapped out full and partial dependencies with transport, IT, plastics/chemicals, waste, shipping and natural capital. Mapping this to financing requirements showed the capital mobilisation, engagement with the sector, data and metrics, policy requirements, technology innovation and value chain partnerships required. Insured, (re)insurers and brokers should all conduct similar exercises and share their needs, insights and learning transparently.

Each of the above case studies gives a broad value chain perspective. However, other examples, such as parametric insurance solutions, catastrophe bonds, tax insurance and supporting insurers in achieving their own transition business plans also exist to help further alleviate the risk management and transfer challenges of the transition.

• Parametric triggers in renewable energy: The transition will require significant renewable energy capacity. As the renewable energy sector continues to develop, renewable energy is expanding into new geographies, some of which will be more susceptible to natural catastrophes. This is likely to create additional physical risks to infrastructure and distribution networks, presenting a key challenge to the development of emerging renewable energy markets.

In a 2023 case study, a leading renewable energy provider in the Philippines worked with Aon to secure parametrictriggered insurance to mitigate risk.^{16,17} The renewable energy provider has a large network of physical infrastructure and distribution centres across the Philippines and was concerned about the potential impact of a catastrophic weather event on its facilities. The country averages 20 storms and typhoons annually, causing millions of dollars in losses as well as disrupting vital public utilities such as electricity services. The local insurance market provides only limited coverage from traditional property damage products for the energy transition and distribution industry. To address this gap, past catastrophic weather events over a two-year period were modelled. A bespoke windstorm model was developed to quantify the infrastructure and property loss at different pre-agreed levels of maximum sustained wind values on a one-to-five scale based on historical pricing. This allowed the development of an appropriate cost for potential damages to the network. As a result, the provider was able to obtain terms for a parametric solution covering windstorm risk, with claim payments designed to match storm proximity and severity. The solution also enabled a quicker and more transparent claims settlement process, which was seen in action in December 2021, when the programme was triggered by Typhoon Rai. In this instance, a payment arrived within 30 days (and within ten days of the programme being finalised).

• Tax insurance for renewable energy: Businesses can work with brokers to manage the wide range of tax risks associated with the renewable energy sector. For example, successful financing of renewable energy developments in the US is contingent on the eligibility of projects for investment tax credits (ITC) or production tax credits (PTC). Tax credits are one of the primary incentives to encourage investment in solar, wind and other renewable energy projects. Institutional investors can provide a source of funding for these projects through mechanisms such as tax equity, whereby a proportion of project costs are covered by investors in exchange for tax credits and cash returns. However, tax equity investors are subject to a number of tax risks. These include the investment structure not being respected, projects not qualifying for the projected tax benefits (including adjustments to the qualified basis) or the loss of tax benefits through recapture.

In such cases tax insurance can provide effective protection against the loss of ITCs or PTCs due to a successful challenge by a relevant tax authority and can be instrumental in facilitating the financing of projects, providing certainty, assurance of tax credit eligibility and credit enhancement. A diversified pool of highly rated insurers can then supplement the developer or sponsor's tax indemnity.

• Supporting insurers' transition business plans: Insurers will be looking for help on their own plans to identify new risk management/risk transfer solutions for potential insureds as the energy transition accelerates. Insurers themselves will need to better understand the capabilities required to meet their underwriting plans related to the transition, ranging from technology and data requirements to ways of adapting operating models.

Section 3: Key recommendations to turn transition challenges into opportunities

As things stand today, the world is set to miss the target set within the 2015 Paris Agreement to limit global warming to no more than 2°C above pre-industrial levels by 2100. We are even further from achieving the stretch target of 1.5°C, which would significantly reduce the impacts of climate change over the rest of the century.

This section sets out recommendations that can help increase the pace of transition, and key participants that need to be involved in delivering the recommended actions.

Figure 5. Summary of recommendations

	Recommendation	For whom
1	Consider project insurance at project inception phase.	BusinessesFinanciers(Re)insurersBrokers
2	Articulate transition plans early to ensure that risk capital remains available and adequate for evolving business operations.	Businesses(Re)insurersBrokers
3	Realign time horizons for insurance from a transactional annual renewal cycle towards a multi-year, multi-stakeholder partnership approach that incentivises innovation and 'patient capital'.	BusinessesFinanciers(Re)insurersBrokers
4	Appreciate that not all risk management and risk (transfer) solutions to transition barriers will be product-based.	(Re)insurersBrokers
5	Go 'back to basics' and embrace uncertainty concerning future liabilities as an <i>advantage</i> for underwriting.	• (Re)insurers • Brokers



Recommendation 1. Consider project insurance at project conception phase

Decarbonisation projects are large and complex, involving a range of technical inputs and development timelines. Given the importance of insurance in attracting finance, a concerted effort by participants along the value chain to consider insurance and risk management is clearly warranted. This demands a front-to-back discussion, involving early engagement between financiers, developers, engineers and designers with their brokers and risk management partners present and involved. The broker relationship allows multiple perspectives to be considered, from different carriers and providers of risk transfer capital, as well as primary insurers and reinsurers, all of whom can concentrate on the problems (data, exposure, etc.) that need to be solved along the value chain for the duration of a transition project. There are five key steps to elevating the management of risk earlier in the process:

- 1. Identify the project timelines and durations involved.
- Identify key value chain participants, including banks, engineering firms, original equipment manufacturers (OEMs), etc.
- 3. Identify key risks for each step and partner along the value chain.
- 4. Develop risk management programme, which includes operational and contractual means of mitigating risk.
- 5. Determine appropriate risk transfer solutions and whether or not they exist or need to be created/modified.





Recommendation 2. Articulate transition plans early to ensure that risk capital remains available and adequate for evolving business operations

The transition to net zero is a process, and this fact is reflected in the framework produced by the Transition Planning Taskforce (TPT), which regulators are looking to as a source of leading practice across multiple markets.¹⁸ It is important to recognise that a transition plan is not simply a disclosure, but a multi-year approach covering all the steps necessary to transition. Insurers, brokers and the customers of these businesses should all be setting out transition plans, whether or not they are made public, and understand the dependencies that exist between the transition plan requirements of the insured, their brokers, insurers/cedants and reinsurers.

This begins with developing an understanding of the future implications and opportunities of climate risk through scenario analysis. While many organisations and insurers have conducted climate scenario analysis exercises, they will become mandatory under the Corporate Sustainability Reporting Directive (CSRD) in the European Union for an increasing number of businesses, as well as in jurisdictions that have committed to adopting the International Sustainability Standards Board (ISSB) framework.¹⁹ Hence, when conducting future scenario analysis, this should directly input into strategic decision-making and help inform the transition plan.

With the development of more comprehensive transition plans across the insurance value chain, insurers are increasingly scrutinising the ESG performance of companies. Additionally, with an increase in greenwashing issues, there needs to be a focus on helping the insured and their insurers forecast their transition strategies and objectives in a transparent manner. Investment in tools that enable insurers to better understand the transition plans of their clients will allow them to differentiate between those taking serious steps towards the transition and those who are not. It will also allow insured organisations in hard-to-abate sectors to better articulate and report progress against their transition targets, bringing a number of additional benefits. Such data needs to be presented in a holistic manner to enable comparison across industries, geographies and business entities. For example, presenting emissions reductions relative to production levels can offer a view of progress that allows for easier comparison between businesses. This approach enhances transparency and encourages better informed decision-making among stakeholders, helping to deliver sustainable outcomes across the energy sector.²⁰

Tools such as the Transition Performance Index (TPI) from Aon use a range of datapoints, including measurements of carbon emissions, to help evidence the trajectory of their clients' climate transition plans. This helps (re)insurance underwriters to better understand their progress against commitments to become greener over time.²¹ In doing so, businesses in hard-to-abate sectors are able to reduce total cost of risk and access the capital needed to accelerate the transition. The greenwashing module within TPI also shows greenwashing resiliency, providing evidence on accuracy and yearly progression towards targeted goals.

Meanwhile, for the insured, consider how you articulate and discuss your transition plans with brokers and insurers to ensure that the risk (transfer) solutions you require for future operations are well understood. Insurers and brokers must ensure that proactive discussions are being held, especially at the top table, with hard-to-abate businesses concerning the risk (transfer) solutions that exist to cater to their current and future risk profiles. This should also include discussion of any risk solutions that may need to be created. These exchanges should be informed by a thorough climate risk assessment to expose all relevant climate risks to which an insured entity is exposed – information that will be crucial to the insurer or broker.

Insurers can further incentivise climate risk adaptation efforts through their underwriting policies, recognising risk reduction measures in businesses with more favourable policy terms that do not necessarily lead to reduced premiums.

When considering transition plans that takes place at an industry and geography level, the traditional silos of product and geography themselves need to be rethought. As has already happened in the power generation sector, this needs to cover construction and warranties, as well as property, with potential enhancements from risk engineering and parametric solutions. Innovation needs to be targeted at the industry and geography in question. For instance, decommissioning will happen at different speeds in different geographies, with the associated risks assessed locally.



Recommendation 3.

Realign time horizons for insurance from a transactional annual renewal cycle towards a multi-year, multi-stakeholder partnership approach that incentivises innovation and 'patient capital'

The insurance industry should consider longer policy terms than the standard annual renewal cycle in certain instances noting that multi-year policies exist for certain areas such as major construction. The ability to provide stable insurance coverage over long periods can free up capital flows and incentivise investment in clean technologies otherwise not investable at scale.²² Project financiers, businesses and other insurance value chain participants should each engage with the specifics of the climate transition solution for each industry or sector they address, collaborating with technical experts such as product engineers and climate scientists from academia and industry. This will help them to identify specific challenges and relevant technological developments. In addition, we see opportunities for sector-wide data sharing and data governance frameworks, helping to deliver faster and more relevant climate-ready risk (transfer) solutions.

Additionally, insurance industry associations at regional and national levels should collaborate more freely with other value chain participants in pre-competitive phases to discuss risk (transfer) solutions and insurable priorities. This will enable learning and experimenting opportunities that in turn will facilitate the pooling of risk and/or the development of new risk solutions that are not dependent on pre-existing data. It will also enable better signalling of emerging risk profiles to the wider risk (transfer) solution ecosystem, helping stakeholders to plan the research and development resources required to enable the wave of further innovation needed around risk management solutions. One notable example is the Understanding Risk Forum which was established in 2010. It represents a global community with around 13,000 members active in the creation, communication and use of disaster risk information for business resilience.²³

Businesses can also create future scenario analyses for their own value chain and transition pathways, which can further inform policy makers and assist multiple stakeholders to partner together more effectively without the appearance of collusion. The semiconductor industry provides a valuable example of how this can work in practice. In this example, industry, academia and government have been working together in a successful partnership for several decades now.²⁴ We also see the beginnings of effective partnerships with actuaries, teaming up with academics to convey the real dangers of climate change in actuarial terms that can help to activate these key stakeholders. This includes the novel concept of 'Planetary Solvency', which actuaries maintain is essential to support long-term policy decisions.^{25,26}





Recommendation 4. Appreciate that not all risk management and risk (transfer) solutions to transition barriers will be product-based

Insurance products may not necessarily be the solution to all conversations around the de-risking of transition projects. The limitations of year-by-year cover associated with insurance products, for example, are not well aligned to the long-term requirements of climate change transition planning.

Insurers and brokers can close coverage gaps through their risk engineering and risk consulting capabilities. This can also help insured parties to better understand the interventions that help secure coverage, which may not be available, and make a stronger case for the underwriter looking at the risk. For insurers, the importance of looking at the insured's business as a whole entity for risk transfer solutions is paramount.

Brokers can play an important role here as the main conduit through which businesses buy insurance. Brokers could potentially be asked to perform due diligence on their clients to make sure that the business they are placing complies with the criteria set out by insurers. Brokers can also proactively engage with clients to help them take steps towards reducing their GHG emissions in order to qualify to purchase a specific insurance policy.

However, this should ideally be predicated on a longerterm relationship that seeks to support the transition plan and decarbonisation goals of the insured, as well as the insurer, enabling a conversation that looks beyond the annual renewal cycle to one where an understanding of the longer-term risk profile helps secure capacity and offers a longer-term perspective for brokers and carriers.

Innovation and front-to-back thinking will not happen without adjustments to incentives and compensation. Traditional insurance models will likely need to adapt, taking a more flexible approach to accommodate the changing risk landscape and innovations required, with risk consulting and advisory services becoming an increasingly valuable element of the risk transfer process.

Nevertheless, due to the immaturity of green technologies, uncertainties will persist around project completion requiring participants within the insurance value chain to adapt and tailor renumeration models accordingly.





Recommendation 5. Go 'back to basics' and embrace uncertainty concerning future liabilities as an advantage for underwriting.

While the lack of relevant historical data could make quantification of climate risks and the validation of predictive models challenging, the insurance industry has a long history of dealing with new risks. This legacy of adaptability will be useful in dealing with climate-related risks. Time and again (re)insurers have managed new uncertainties, from developing policies that cover COVID 19 risk to dealing with the complex challenges presented by cyber-crime, to providing coverage for intangible assets like intellectual property and carbon credits.

Utilising a wider range of data sources can help insurers and businesses develop a more customised view of risk. The use of multiple data sets and models can also help solve challenges around unpredictability as well as variances in assumptions at geographical levels.²⁷ Actuaries and data scientists have taken this challenge on already, constructing realistic scenarios in collaboration with climate scientists and systems thinkers to communicate uncertainty and provide a realistic outlook of the changes to come.²⁸ Meanwhile, tools such Aon's Climate Risk Monitor, for example, use state-of-the-art climate model projections to inform historical and future assessments of physical climate risk. The analysis generated helps businesses better prioritise and understand their climate position in order to make more effective long-term decisions around building resilience, shoring up investments and adequately transferring risks.²⁹

In addition, innovations such as parametric insurance as a complement to traditional risk solution programmes can help to better match capital to the broad nature of risks caused by climate-related disasters.³⁰

Parametric solutions cover the occurrence of a loss-causing climate event happening instead of indemnifying the actual loss incurred from the event. While parametric insurance has an established track record in many countries, some regulatory and legal uncertainty remain.^{31,32} The role of governments (see Section 2) and their national climate mitigation and adaptation teams working alongside insurance value chain participants is therefore crucial to ensuring innovations such as parametric insurance can be accessed in multiple geographies at scale.

Given the shared goal insurers have, and the commercial nature of insurance, partnerships between competitors might seem unusual. Yet in the semiconductor industry, for example, we see that, in practice, there is considerable space for providers to work together, with collaboration and competition coexisting in the pursuit of a shared goal.³³ The chemicals sector offers a useful example of such partnering, with the industry encouraging the use of green chemistry to encourage chemists to reduce the health, safety and environmental impacts of chemical products and processes across the industry.³⁴

It is clear that underwriters and risk managers themselves have the power to galvanise and drive meaningful, collective change up and down the value chain, further cementing their role as key players in the global climate transition.

Conclusion

The risk (transfer) solution industry is a critical enabler of the climate transition, one that can prevent unintentional delays in the global shift towards a lowcarbon future. It is becoming increasingly important to find ways to combine risk, engineering and financial acumen more effectively to better manage the risks associated with climate change.

Better and more integrated strategies are needed from project financiers, businesses and insurance value chain participants too, to create more bankable projects and optimise risk transfer as part of new project financing solutions.

There is already broad agreement that the cost of inaction will greatly outweigh the cost of action. All stakeholders should be wary of well-trodden paths, reassess their contributions to solving this collective issue, and remain open to working and learning together. This is crucial to ensure that risk management, risk (transfer) solution providers, and the insurance industry can effectively contribute to building security and prosperity for society and, together, solve the global climate change challenge.



Glossary

Agribusiness	Commerce in farming and farming-related activities covering the production, processing and distribution of farm-based goods.
Blue hydrogen [See green hydrogen]	The carbon-neutral process of extracting hydrogen from natural gas mixed with very hot steam and a catalyst. A chemical reaction occurs creating hydrogen and carbon monoxide. Water is added to the mixture turning the carbon monoxide into carbon dioxide (CO_2) and more hydrogen. The CO_2 emissions are captured and stored underground.
Capital expenditures	Funds used by a company to acquire, upgrade and maintain physical assets such as property, plants, buildings, technology or equipment.
Climate transition plan (the 'transition')	A time-bound action plan that clearly outlines how an organisation will pivot or adapt its existing operations, assets and business models towards a trajectory that aligns with the latest climate science recommendations of reaching net zero by 2050 and thereby, limiting global warming to 1.5°C.
Decarbonise	Reduce or eliminate carbon dioxide emissions from a process (such as manufacturing or the production of energy) or in the environment.
Green hydrogen [See blue hydrogen]	The production of hydrogen through the electrolysis of water using renewable energy resulting in low- carbon emissions and no requirement for carbon capture facilities.
Green technology	The use of innovative technologies to create products and services that mitigate against and/or reverse human impact on the environment.
Hard-to-abate sectors/ industries	Sectors and industries with relatively high greenhouse gas emissions such as aviation, shipping, road transport, agriculture and food production, chemicals and steel that have few clear, viable low-emission alternatives.
Involuntary transition	Regulatory mandates or nature loss and degradation requiring businesses to develop and execute a strategy in the move towards a low-carbon economy.
Parametric insurance	An insurance solution that covers the likelihood of a loss-causing climate event happening instead of indemnifying the actual loss incurred from the event. It is an agreement to make a payment upon the occurrence of a covered event meeting or exceeding a pre-defined intensity threshold, as measured by an objective value (or parameter).
Risk pool	A group of insurers or reinsurers (the 'pool') through which particular types of risks are underwritten, with premiums, losses and expenses shared in agreed ratios.
Risk transfer	The transfer of exposure to potential loss from adverse outcomes (i.e. the risk) to another party.
Value chain	A series of consecutive steps that a business performs in order to deliver goods and/or services to an end customer.
Voluntary transition	A business voluntarily developing and executing a strategy in the move towards a low-carbon economy.
Warranties	Guarantees issued by a seller of a good/service to a buyer that a product or service will meet certain specifications.

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29

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