

BUILDING A GLOBAL AGRICULTURAL INSURANCE MECHANISM UNDER THE UNFCCC

by

Joab J. L. Osumba

Climate Smart Agriculture Component

Finance Innovation for Climate Change Fund

Matrix Development Consultants

Africa-Asia Conclave on Loss and Damage due to Climate Change:

Instituting a Global Agricultural Insurance Programme as a Risk Sharing and Transfer Mechanism for Developing Countries

Eastland Hotel Nairobi

25-26 August, 2016

- Insurance is one of the “approaches to address loss and damage associated with the adverse effects of climate change” – as provided for under UNFCCC
- A proposal for a catastrophe insurance facility (by AOSIS in 1991) preceded the debate on loss and damage negotiations under UNFCCC
- Discussion on Loss and damage was formally initiated under the Bali Action Plan (decision 1/CP.13) in 2007
 - later embedded in the Cancun Adaptation Framework (1/CP.16) in 2010
 - further elaborated on in Durban (8/CP.17) and Doha (3/CP.18).
- Loss and damage is a consequence of the lack of ambitious efforts to reduce emissions and address adaptation needs, thereby triggering climate-related disasters

- The work programme on loss and damage has been enhancing knowledge and understanding on insurance solutions among other approaches to address loss and damage
 - Thematic area 2 of the work programme on loss and damage recognizes “A range of approaches to address loss and damage”
- Current operational documents for loss and damage include the Paris Agreement (2015) and WIM for Loss and Damage (2014), which
 - Acknowledged **ongoing initiatives** relevant to loss and damage;
 - Acknowledged the **need to enhance support**, including finance, technology and capacity-building, for relevant actions;
 - Agreed that comprehensive, **inclusive** and **strategic** responses are needed to address loss and damage

Building a Global Agricultural Insurance Mechanism **under the UNFCCC**

1. What is the feasibility of a global agricultural (crop and livestock) insurance mechanism **under the UNFCCC**?
2. What are the opportunities, challenges and risks involved in creation of such a mechanism?
3. How do we ensure that such a mechanism can be fair, affordable and effective agricultural insurance mechanism which can help to build resilience to farmers in the developing countries?

mechanism under the UNFCCC

- There's nothing in the Paris Agreement text that requires specific reductions by specific countries within specific periods, he said, **leaving open the possibility that mitigation and adaptation efforts will progress too slowly**
- There are provisions in the texts of the WIM and the Paris Agreement that allows for the establishment of such a mechanism
 - The preamble of the Warsaw decision on loss and damage recognizes that loss and damage in some cases involves more than that which can be reduced by adaptation
- Insurance solutions are recognized in the Paris Agreement under loss and damage
 - Para 49: In the Paris Agreement Parties *request* the ExeCom of the WIM to establish **a clearinghouse for risk transfer** that serves as **a repository for information on insurance and risk transfer**, in order to facilitate the efforts of Parties to develop and implement comprehensive **risk management strategies**
 - Article 8: Parties also recognize that “areas of cooperation and facilitation to enhance understanding, action and support may include ... **Risk insurance facilities, climate risk pooling and other insurance solutions**”
- Insurance funds are available faster, and can be used more flexibly, than aid funds

- Insurance has been in the agenda of The ExeCom of the WIM, and will be reported on at COP22, where the WIM work plan will be reviewed
 - Stocktaking in COP 22 in November on the mandate, structure and effectiveness of the Warsaw International Mechanism
- In the WIM the COP acknowledges the contribution of ... “**risk management strategies**” towards addressing loss and damage
- The COP further decides that the WIM shall promote the implementation of approaches to address loss and damage by “**providing information and recommendations for consideration**” by the COP when providing guidance relevant to reducing the risks of loss and damage.
- Insurance features strongly in the existing financial instruments as contained in the submissions by agencies to the ExeCom of WIM
 - Parties and organizations have reported experience with and lessons from a variety of financial instruments and tools that may be applied to raise and channel this finance at all levels

- A range of insurance approaches have been piloted in different regions (including sovereign risk pilots) at regional/national level indicate a strong interest in agricultural insurance related to loss and damage
 - The instruments have been applied at different levels depending on where reported action to address climate risk is taken.
 - There are proven best-bet practices among pilot initiatives that need scaling up/ scaling out and replicating
 - all the pilots show strong interest in the concept by the vulnerable communities
 - They could serve to establish an enabling policy or regulatory environment for agricultural insurance
- IPCC-5AR recommends insurance solutions, among other interventions, for unavoided or unavoidable loss and damage, for example in places that become uninhabitable or unproductive because of climate change impacts, or for people living in places where risks of livelihood failure or loss and damage to assets due to climate-related events becomes intolerable.
- In recent years, index-based insurance solutions have emerged that can be instrumental in addressing such losses and avoiding the uptake of erosive coping strategies that undermine future livelihood sustainability and perpetuate social vulnerability.

Opportunities available for the mechanism

- The concept of loss and damage originated from a push for an insurance facility within the UNFCCC Framework, and the drive is still alive
- Warsaw International Mechanism (WIM) is recognized in the Paris Agreement
- the Paris Agreement included anticipatory mechanisms through risk insurance; and assured the continuation of the WIM
- Article 8.3 notes that, “Accordingly, areas of cooperation and facilitation to enhance understanding, action and support may include “Risk insurance facilities, climate risk pooling, and other insurance solutions”
- G7 Climate Risk Insurance Initiative, which plans to address loss and damage through insurance solutions, is understood to have very high political goodwill
- Report/results/findings of the Warsaw Mechanism’s three-year mandate, to be presented at COP22 in Marrakesh 2016, will come in handy

Opportunities available for the mechanism

- Warsaw Mechanism will be further examined in Marrakesh, including its structure, effectiveness, and mandate
 - Work plan for the ExeCom of the WIM for the next 5 years will be a good place to anchor this effort
- One of the steps for the ExeCom of WIM was to determine what the appropriate responses are:
 - whether they involve reducing barriers that make it hard to plan and implement adaptation,
 - or implementing approaches to manage when limits to adaptation are crossed
- In Decision 2/CP.20 para 8, COP20 decided that the ExeCom may establish expert groups, subcommittees, panels, thematic advisory groups or task-focused ad hoc working groups to help execute the work of the ExeCom in guiding the implementation of the WIM, as appropriate, in an advisory role

Opportunities available for the mechanism

- UNFCCC, under the Bali Action Plan and the Cancun Agreement, recognizes insurance as a risk transfer mechanism
 - Cancun Agreement proposes the development of a climate risk insurance facility to address impacts associated with severe weather events, including options for micro-insurance
- Under Action Areas 2 & 7 of the initial two-year work plan of the mechanism, the Executive Committee of the Warsaw Mechanism on Loss and Damage identifies insurance as one of the financial instruments to facilitate comprehensive risk management
 - The workplan stresses the importance of enhancing and developing measures such as insurance, and encouraging institutions to incorporate them as part of development projects and investment criteria
- **international experience** suggests that sustainable agriculture insurance, especially for small-holder farmers, requires both government and private sector support
- Decision 1/CP.21 requests the ExeCom of WIM to establish a clearinghouse for risk transfer (**usually including insurance**) that:
 - Provides a repository for information on insurance and risk transfer;
 - Assists Parties in ... finding best insurance schemes

- Paris Agreement decided on the continuation of the WIM for LD, following its review in 2016, and requested the ExeCom to:
 - Establish a clearing house for **risk transfer** that serves as a repository for **information on insurance and risk transfer**, in order to facilitate the efforts of Parties to develop and implement comprehensive **risk management strategies**
 - Establish a **task force** to complement, draw upon the work of and involve, as appropriate, existing bodies and expert groups under the Convention including the Adaptation Committee and the Least Developed Countries Expert Group, as well as relevant organizations and expert bodies outside the Convention, **to develop recommendations for integrated approaches** to avert, minimize and address displacement related to the adverse impacts of climate change
- Regional initiatives such as ARC and HARITA can be emulated and coalesced
 - Lessons learnt from regional/national pilots in various regions can be built on

- Paris Agreement treats loss and damage separately from adaptation but WIM for Loss and Damage is placed under the Adaptation Framework
- Many of the financial instruments piloted so far still have serious limitations
- High premium rates, due to uncertainty occasioned by
 - data scarcity – production and climate data
 - Increased frequency and severity of occurrence of insurable risks
 - lateness in assessing risks
 - slow flow of climate funds
 - basis risk due to increased weather variability
- Availability of sufficient resources for the successful and timely implementation
 - the question of who contribute to the subsidy kitty

- Market failures: market imperfections that may affect the effectiveness of insurance
- Market barriers (information asymmetries causing moral hazard and adverse selection, transaction costs, enforcement constraints, and ambiguity aversion) and availability of alternative measures including humanitarian aid constrain development of new insurance markets
 - Inadequate flow of information: **asymmetric information** (e.g. about the risk profile of properties) and **moral hazard** (e.g. for people with insurance coverage or with at-risk communities holding out for government assistance)
 - inertia, procrastination due to behavioural and information barriers
 - Low insurance penetration
- Institutional gaps at the regional, national and local levels in particularly vulnerable developing countries to promote integration and coherence in a manner that is country-driven
- Weak coordination among stakeholders
- Shortage of technology, capability and capacity for data gathering and knowledge management on agricultural insurance

- Private schemes without subsidies might be unaffordable for poorer households and small enterprises especially in highly vulnerable regions where premiums need to be high
- Inadequate monitoring and observation of weather parameters, indexing of thresholds, awareness raising, inadequate guidelines, and lack of advocacy and coordination among agencies in the process of design and implementation
- Weak financial and technical capacity of vulnerable developing country Parties
- Weak capacity of national re-insurers in vulnerable developing country Parties to rise to the challenge
- Systems for data collection are rudimentary and building them will require time
- Farmers may be covered for all production risks but could still suffer from the impact of price shocks

- The slow pace of reaching desired negotiated outcomes
- Failing to get adequate support to implement the scheme: Require high level of cooperation
- Insurance subsidy, relevant to insurance mechanism, may become a sticking point
- Interpretation of wording in the WIM and Paris Agreement text may drag debate for longer than desired
- Insurance under loss and damage has been seen by some as a mere liability/ compensation/ pay-out mechanism, and may continue to be seen as such
- There is no mention in the concept note on how it will be anchored in the WIM and in the Paris Agreement at COP22
- Insurance was not expressly mentioned in the Warsaw Mechanism but was included in the initial work plan of the Executive Committee of the Mechanism.
 - could bring negotiation challenges
 - Executive Committee of WIM may not admit it into their report if they have not been consulted

- There is no guarantee that the new policy space created by WIM will deliver new ways of framing the issues
- Focus is now on implementing the Paris Agreement - new negotiations may not be welcome after Paris
- There is potential for argument that it will be a mechanism within a mechanism (like happened with loss and damage versus adaptation)
- Resources may not be available when needed: **Those who need to pay may refuse to pay** – Subsidy may be a long and winding debate

The case for a fair, affordable, effective agricultural insurance mechanism

The “fairness” criteria: The principle of “equity”

- *TRANSPARENCY OF ACTION AND SUPPORT* under the Paris Agreement (*decides* to establish a Capacity-building Initiative for Transparency in order to build institutional and technical capacity, both pre- and post-2020)

Finding Fair Criteria

- Decision criteria for fairness
 - Objectivity
 - Transparency and accountability
 - Affirmative action
 - Capacity building to seize opportunities
 - Best practice
 - Equality of say, including the right to say “No”.
 - Mutuality of respect
 - Laws, rules, regulations,, norms, standards
 - Advisory opinions of respectable minds

The “affordability” criteria

- Subsidy
- Flexibility - learn and adjust
- Differentiation – a product for each segment
- Decisions derived from the most recent data gathered, within the levels specified
- Collaboration to enhance synergy
- Economies of scale

The “effectiveness” criteria

- Accessibility, cost, user satisfaction, cost/benefit ratio
- Structures for implementation
- Speed/response time of
 - approval
 - clearing
 - availability of funds
 - settlement among depository institutions/ account providers
 - visibility of initiatives
- Quality of service
- Surveys – to learn and adjust

- It is feasible to establish a global agricultural (crop and livestock) insurance mechanism **under the UNFCCC**
- Opportunities exist for establishing such a mechanism, but challenges and risks are also anticipated
- Issues of fairness, affordability and effectiveness are crucial in establishing the mechanism to help build resilience to farmers in the developing countries
- Political pragmatism, genuine negotiation and compromise will be required

- Frame the mechanism as a new way of viewing the climate change challenge, for instance by providing evidence where adaptation and DRR have fallen short
- Gather sufficient diplomatic momentum for a decision in Marrakesh
 - build the insurance case around “beyond adaptation” debate
 - Build a case around the risk diversification and resilience building functions of insurance
- Emphasize the role of insurance at the review of WIM for LD at COP22 to anchor it in the mechanism, in conjunction with other agricultural risk management measures

END

Thanks