

Mitigating environmental, social and governance (ESG) risks in underwriting and investment management





Table of contents

1. Introduction and purpose	4
2. Roles and responsibilities	6
3. ESG approach	6
3.1 Our code of conduct	6
3.2 Risk management	6
3.3 ESG in investment practices	7
3.3.1 Exclusions	8
3.4 ESG in underwriting	8
Zurich's position on:	
3.4.1 Human rights	9
3.4.2 Dam construction, mining and oil and gas	10
3.4.3 Banned cluster munitions and anti-personnel land mines	10
3.4.4 Thermal coal	11
3.5 Applying this approach	11
4. External commitments	11

Purpose

1. Introduction and purpose

We work with our customers, brokers and other distribution partners to ensure responsible and sustainable business practices and to protect reputation, while promoting best practices in managing environmental, social and governance (ESG) risks.

Our aim is to promote international best practice standards that help ensure that potentially adverse ESG impacts are adequately managed.

Why it matters

Society is facing increasingly interconnected and complex ESG challenges. The insurance industry cannot be a bystander and where appropriate, it must play its role in addressing these challenges as a manager of risk. Failing to do so, can have a damaging effect on society, stakeholder trust and the reputation of the insurance industry and its customers. That is why we work with our corporate customers and brokers to better manage ESG risks and strive to promote best practices in managing these risks.

Engaging with customers

We integrate our commitment to corporate responsibility and the UN Global Compact in our underwriting and business decisions. We believe it is better to engage with customers to understand their business and operations, and work together to ensure responsible and sustainable business practices are in place.

This enables us to make better-informed decisions on how we can support customers in developing best practice.

A three-step approach that systematically detects risks

Zurich uses a three-step approach that systematically detects, assesses, and mitigates major ESG risks that are inherent in specific business transactions. Concerns about risks can be escalated to a corporate responsibility decision group (CR Decision Group) to assess sensitive or complex ESG risks and provide direction as to the appropriate mitigation actions. We track and analyze the outcome of risk assessment and risk mitigation efforts.

Our risk-profiling methodology

Using our proprietary risk-profiling methodology, we have prioritized five key areas of concern: thermal coal; banned cluster munitions and anti-personnel land mines; and governance, human rights and environmental risks in dam construction, mining, and oil and gas activities.

For each of these areas of concern, we have drawn up an issue brief that sets out our position and best practices. We also provide guidance and training for underwriters and other relevant stakeholder groups, and have established ESG risk assessment and referral processes.

Being a responsible investor

We believe that proactively integrating ESG factors in our investing will help us to do our job well on a long-term basis. ESG integration – across asset classes, and alongside traditional financial metrics and state-of-the-art risk management practices – helps us to achieve superior risk-adjusted, long-term financial returns.

This document serves to outline Zurich's approach in addressing ESG issues in both underwriting and investing.



Description

2. Roles and responsibilities

For all corporate responsibility (CR) areas, the Executive Committee and the Board take an active role in overseeing and implementing our approach. The Governance, Nominations and Corporate Responsibility Committee, a standing committee of the Board, reviews and approves the Group's CR strategy and objectives and a CR Working Group ensures we achieve our CR objectives. Sensitive or complex CR risks can be escalated to the CR Decision Group.

Governance, Nominations and Corporate Responsibility Committee

In 2016, the Governance and Nominations Committee's mandate was extended to include corporate responsibility more broadly, reviewing and approving the Group's corporate responsibility strategy and objectives. The committee, which meets at least twice a year, consists of the five directors and is chaired by the Chairman of the Board.

CR Working Group

The CR Working Group, set up by the Executive Committee, ensures that we achieve our CR objectives. The Working Group comprises senior representatives from across the business and is chaired by the Chief Executive Officer, Europe, Middle East & Africa.

Corporate Responsibility Decision Group

With regard to ESG issues in business transactions, concerns about underwriting risks can be escalated to a Corporate Responsibility Decision Group to assess sensitive or complex corporate responsibility risks and provide direction as to the appropriate mitigation actions. This group includes senior members of relevant business areas, compliance and risk.

3. ESG approach

3.1. Our code of conduct

Zurich's code of conduct articulates our values and the key rules of conduct by which we abide to help ensure that we conduct our business activities in accordance with the highest ethical, legal and professional standards.

Zurich's code of conduct applies to all employees of Zurich, its subsidiaries and affiliates worldwide. In addition, third parties who work on Zurich's behalf, such as consultants, advisers, service suppliers, or agents, must comply with the provisions of Zurich's code of conduct as specified in their contractual agreements with us.

3.2 Risk management

Taking risk is inherent to the insurance business, but such risk-taking needs to be made in an informed and disciplined manner, and within a pre-determined risk appetite and tolerance.

The major risk management objectives at Zurich are to:

- Support achievement of the Group strategy and protect capital, liquidity, earnings and reputation by monitoring that risks are taken within the Group's risk tolerance
- Enhance value creation by embedding disciplined risk taking in the company culture and contributing to an optimal risk-return profile where risk reward trade-offs are transparent, understood, and risks are appropriately rewarded
- Efficiently and effectively diversify risk and mitigate unrewarded risks
- Encourage openness and transparency to enable effective risk management
- Support decision-making processes by providing consistent, reliable and timely risk information
- Protect Zurich's reputation and brand by promoting a sound culture of risk awareness, and disciplined and informed risk taking.

Zurich has a global and interdisciplinary Emerging Risks Group (ERG) which looks at potential risks for customers, using tools such as the Zurich Risk Radar. Topics on the Zurich Risk Radar are researched by ERG members and the risks and opportunities identified are classified and ranked. The ERG reviews global emerging risks in four groupings; science & technology, legal & regulatory, social trends and environment. The outputs of the ERG provide in-depth assessments at a Group level and also on risks and opportunities for lines of business and underwriting products.

3.3 ESG in investment practices

Every investment involves risk and opportunity. Our aim is to generate maximum return through the risk we are willing to take, and Zurich has always invested its premiums according to this principle. Over the years, we have developed a sophisticated framework for managing our portfolio. Traditional tools used to assess risk and return are based on information that can be easily quantified, and aggregated from balance sheets or income statements.

Unfortunately, this type of reporting does not always provide a complete picture. Our focus on responsible investment has led us to view ESG factors as key considerations to be included when assessing individual investments.

We work closely with our internal and external managers to make sure that the following four basic requirements for ESG integration are reflected in their investment approach:



Training: Raising awareness and teaching investment professionals how to use ESG

A large number of ESG factors can potentially affect risk and return; the channels through which such factors can exert influence are at times complex and vary from sector to sector. All other things being equal, it is riskier to own equity or bonds of a company that, for example, produces excessive greenhouse gas, treats its employees poorly or does not provide information on how it pays its directors, than it is to have exposure to a company that does not do such things. Likewise, it is more rewarding to invest in a company that helps society, benefits the environment and is well governed, or to invest in a real-estate asset that attracts tenants by minimizing energy consumption and greenhouse gas emissions.

It is important for portfolio managers to receive adequate and regular training to help them understand the economic importance of ESG. That is why all Zurich's investment professionals receive responsible investment training.



Information: make ESG data, research and analysis accessible to investment decisions makers

To reflect ESG issues in investment decisions, portfolio managers need access to relevant information in the form of ESG analysis, ratings, and data. At Zurich, we have integrated ESG information into our systems and can retrieve information about ESG performance of our portfolios at our fingertips. In addition, our in-house portfolio managers and analysts have direct access to the ESG research and analysis sourced from specialized providers.



Process integration: reflect ESG in the way portfolios are constructed

The process by which ESG considerations are reflected in decisions to buy/sell, or overweight/underweight a certain security or asset needs to be clearly understood. This process should be documented and consistently applied.

Each manager and team will have to define an approach that fits a specific investment strategy. For a description of the tools, policies, and procedures that we apply to make sure that ESG factors are indeed fully integrated in the investment process and in day-to-day investment decision-making, please consult the [Zurich white paper](#).



Active ownership: the purchase of an asset marks the beginning, not the end of responsibility

Asset managers are expected to execute proxy votes actively, based on best-practice policies addressing ESG issues, and to integrate relevant ESG issues in discussions with companies in which we invest, either as part of regular meetings or through separate channels. Read Zurich's proxy voting policy [here](#).

3.3.1. Exclusions

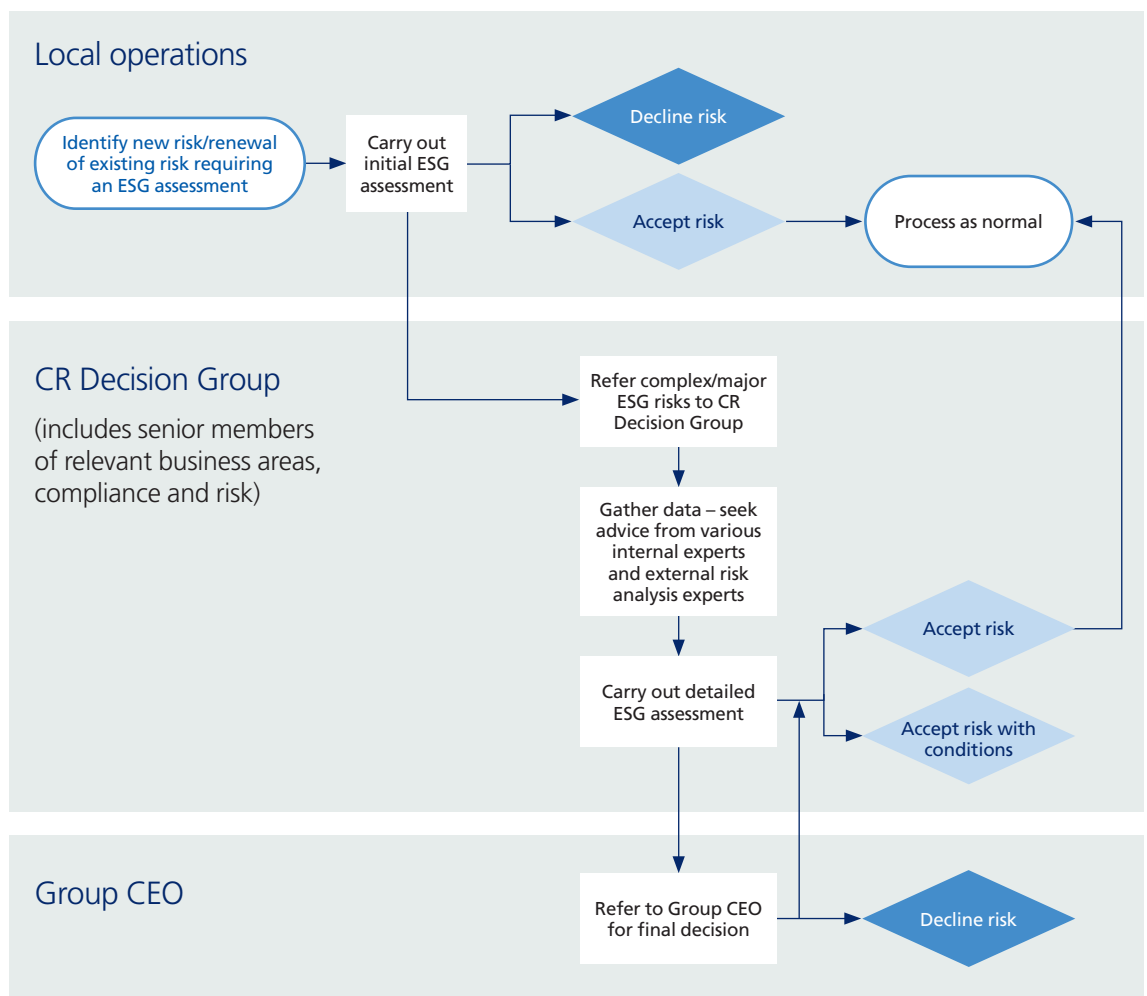
We believe that ESG risks and opportunities are best managed through an ESG integration approach. That being said, there are certain areas where we believe exclusion criteria are justified. Zurich does not engage in any business with, or directly invest in, a number of companies involved in the production of cluster munitions and anti-personnel landmines.

To actively support the transition to a low-carbon economy, Zurich will apply an enhanced ESG risk screening criteria for investments in thermal coal companies. The company will divest from equity holdings in companies that derive more than half of their revenues from mining thermal coal, or utility companies that generate more than half of their energy from coal. It will not invest in new debt issued by such companies and will run off existing holdings.

3.4 ESG in underwriting

As mentioned in the introduction, we work with our customers, brokers and other distribution partners to ensure responsible and sustainable business practices and to protect reputation, while promoting best practices in managing ESG risks.

The process for reviewing ESG risks in business transactions



3.4.1 Zurich's guidelines on human rights

At Zurich, we pay special attention to transactions that might contravene human rights. These are transactions that could serve to:

- Contribute to human rights abuses such as involuntary relocation of local communities, inappropriate use of force or adverse impacts on vulnerable indigenous people.
- Support regimes, governments, government officials or other politically exposed persons in countries with poor governance (for example failed states, conflict or war zones, and ineffective rule of law) or poor human rights records.
- Enable harmful child labor, forced labor, poor health and safety conditions and unfair remuneration.

Our code of conduct

Our commitment to respect human rights is part of Zurich's code of conduct:

- We respect the protection of international human rights within our sphere of influence, and will make sure that we are not complicit in human rights abuses.
- Zurich does not tolerate discrimination or harassment in the workplace on the basis of age, disability, ethnicity, national origin, gender, race, color, religion, marital status, sexual orientation or any other perceived differences.
- Zurich recognizes the right of employees to freedom of association and collective bargaining. All employees have the right to freely form and join groups for the promotion and protection of their employment interests.
- Zurich does not tolerate any form of forced or compulsory labor or child labor.
- The above principles are in accordance with the internationally recognized core employment standards of the International Labour Organization.

United Nations Global Compact

By signing the United Nations Global Compact in 2011, we are committed to aligning our strategy, culture and day-to-day operations with the Global Compact's 10 universally accepted principles in the areas of human rights, labor, environment and anti-corruption. Six of the ten UN Global Compact principles relate to human rights.





3.4.2 Dam construction, mining, oil and gas

Governance, human rights and environmental risks in dam construction, mining, oil and gas.

Dam construction

Dams help communities and economies manage water resources for food production, energy generation, flood alleviation and domestic and industrial use. But they can also displace communities, cause adverse environmental impacts and create the inequitable distribution of benefits.

Oil and gas

The oil and gas sector is an important part of the global energy mix; it provides energy that people, organizations and businesses around the world depend on and has played an important role in improving living standards globally. However, irresponsible management of activities can adversely impact the environment, host communities and countries.



Mining

Mining provides minerals and metals that underpin economic growth and social welfare. If not managed responsibly, mining operations can have adverse impacts on the environment, host communities and countries.

Raising risk awareness

We pay special attention to ESG risks that may:

- directly contribute to human rights abuses, such as involuntary relocation of local communities and support of regimes with poor human rights records
- adversely affect water quality and access to water in neighboring states
- take place in countries with poor governance, such as failed states, conflict or war zones, ineffective rule of law, or poor human rights records
- take place in sensitive ecosystems with a high biodiversity value
- cause damage to protected areas or critical natural habitats.

3.4.3 Banned cluster munitions and anti-personnel land mines

Our stakeholders and society in general are rightly concerned about the production, sale and use of banned cluster munitions and anti-personnel land mines. They cause immeasurable suffering and also expose customers and us to a loss of trust with stakeholders as well as reputational damage.

New business: we do not enter relationships with companies that produce, distribute or market banned cluster munitions or anti-personnel land mines.

Existing customers: we engage in dialogue with customers to explain our position and the related reputation risk and strive for a constructive outcome.

3.4.4 Thermal coal

On December 12, 2015 the parties to the UN Framework Convention on Climate Change reached a new accord, the Paris Agreement, to combat climate change and to accelerate actions needed to secure a sustainable, low carbon future. The agreement calls on all parties to reduce emissions of greenhouse gases, including CO₂, as quickly as possible to restrict global warming to 2 degrees Celsius above pre-industrial levels. One way in which this reduction can be achieved is by finding new alternatives to thermal coal burned to generate electricity, which today accounts for roughly a third of global CO₂ emissions.

Insurers can play a role in facilitating this generational transition towards cleaner energy by increasingly reflecting the climate-related risks inherent in thermal coal in their underwriting and investment policies.

Zurich intends to stop providing insurance or risk management services for new thermal coal mines or for potential new clients that derive more than half their revenue from mining thermal coal, and also for utility companies that generate more than half of their energy from coal. This decision will not apply to workers compensation or other employee protections.

Zurich will apply enhanced risk screening for new or existing clients that derive 30 percent to 50 percent of their revenues from mining thermal coal, or utility companies that generate 30 percent to 50 percent of their energy from coal. The hope is that this additional level of dialogue will identify risk-relevant means of accelerating the transition, like new technologies or emerging best practices.

Lastly, Zurich will engage those clients that derive more than half of their revenues from mining thermal coal or utility companies that generate more than half of their energy from coal in a risk-based dialogue – not to exceed 24 months – with the aim to drive a deeper discussion regarding their mid- to long-term transition plans. Depending on the outcomes of these dialogues, Zurich will either facilitate a transition to an alternative insurer, or explore whether an underwriting exception should be granted based on the client's strategy and position on climate risk.

3.5 Applying this approach

Building a sports stadium in Asia

Zurich was approached to insure construction of a sports stadium, however there were concerns regarding human rights issues of the migrant workers. Our approach to ESG issues in business transactions is to engage with customers to understand their business and operations, and work together to ensure responsible and sustainable business practices are in place. By doing so, we can have a positive influence. We agreed to offer to underwrite the risk by pro-actively working with the customer to ensure appropriate labor standards on the construction site. Also, we applied all of our own anti-bribery and corruption controls to the transaction with the customer and asked the customer to confirm that they had applied similarly rigorous anti-bribery and corruption standards to their dealings with the contracting party.

Going beyond ESG ratings

Zurich's investments include one in a company in the leisure travel business that has a poor ESG rating due to a poor safety record, and substandard labor management practices. The portfolio manager decided to investigate further to better understand these concerns by participating in investor calls, conducting research and engaging with the management of the company directly. Based on this additional information, the manager concluded that ESG issues were effectively addressed and improvements on environmental performance suggested adequate awareness of ESG issues by management.

4 External commitments

United Nations Global Compact

Zurich became a signatory of the United Nations Global Compact in July 2011 because we believe that being a responsible company is fundamental to our long-term sustainability. As a signatory, we are committed to aligning our strategy, culture and day-to-day operations with the Global Compact's 10 universally-accepted principles in the areas of human rights, labor, environment and anti-corruption. The principles of the Global Compact complement our principles, values and code of conduct, and all Zurich employees are expected to live up to them.

Principles for Responsible Investment (PRI)

Zurich has been a signatory of the United Nations-backed Principles for Responsible Investment (PRI) since 2012. The PRI Initiative, a non-profit organization created in conjunction with the United Nations Environment Programme Finance Initiative and the UN Global Compact, is a network of institutional investors, asset managers and service providers working together to put the Principles for Responsible Investment into practice and to share and promote best practice in responsible investment.

UNEP FI Principles for Sustainable Insurance

The United Nations Environment Programme Finance Initiative (UNEP FI) Principles for Sustainable Insurance (PSI) serve as a global framework for the insurance industry to address ESG risks and opportunities. Zurich became a signatory in 2017.

Disclaimer and cautionary statement

This publication has been prepared by Zurich Insurance Group Ltd and the opinions expressed therein are those of Zurich Insurance Group Ltd as of the date of writing and are subject to change without notice. This publication has been produced solely for informational purposes. All information contained in this publication have been compiled and obtained from sources believed to be reliable and credible but no representation or warranty, express or implied, is made by Zurich Insurance Group Ltd or any of its subsidiaries (the 'Group') as to their accuracy or completeness. This publication is not intended to be legal, underwriting, financial, investment or any other type of professional advice. The Group disclaims any and all liability whatsoever resulting from the use of or reliance upon this publication. Certain statements in this publication are forward-looking statements, including, but not limited to, statements that are predictions of or indicate future events, trends, plans, developments or objectives. Undue reliance should not be placed on such statements because, by their nature, they are subject to known and unknown risks and uncertainties and can be affected by numerous unforeseeable factors. The subject matter of this publication is also not tied to any specific insurance product nor will it ensure coverage under any insurance policy. This publication may not be distributed or reproduced either in whole, or in part, without prior written permission of Zurich Insurance Group Ltd, Mythenquai 2, 8002 Zurich, Switzerland. Neither Zurich Insurance Group Ltd nor any of its subsidiaries accept liability for any loss arising from the use or distribution of this publication. This publication does not constitute an offer or an invitation for the sale or purchase of securities in any jurisdiction.