

# The Willis Index

Willis

## Environmental Newsletter

The Environmental Insurance and Risk Management Quarterly

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## Environmental Risk and Insurance

Environmental risk is notoriously difficult to accurately quantify, verify and manage. In particular, it creates difficulties in predicting the timing and quantification of the associated liabilities, and thus the evaluation of appropriate financial provision. Environmental insurance is increasingly used as an effective mechanism to transfer environmental liabilities associated with corporate and property transactions as well as ongoing operations.

### What is environmental insurance?

Environmental insurance is a specialist form of insurance providing cover against losses that could be incurred as a result of third party and regulatory action arising from pollution or contamination.

### What do policies cover?

Environmental insurance policies cover statutory clean-up requirements, third party claims for bodily injury and property damage, and associated legal expenses, resulting from pollution or contamination events, whether such events are "sudden and accidental" or "gradual" in nature. Related costs such as business interruption losses (e.g. loss of profit, loss of rental income) can also be covered.

### What are the main policies available?

The principal environmental insurance coverages, which can be tailored to meet the specific risk, are:

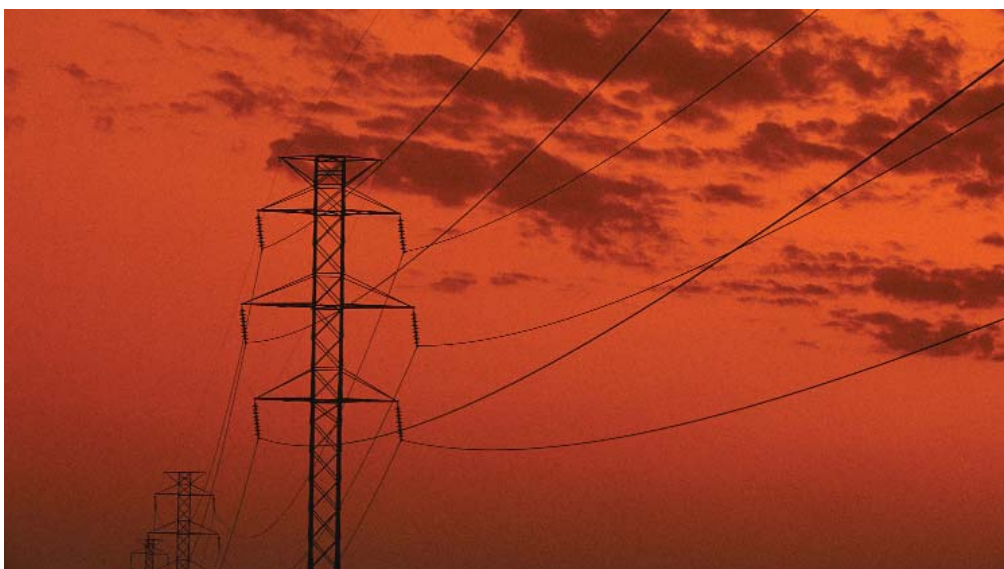
- Historical Pollution Cover: Arranged for liabilities associated with pre-existing contamination (e.g. due to previous industrial operations) or for contingent liability exposures associated with previous divestments.
- Operational Pollution Cover: Cover for ongoing pollution risks, for example from unanticipated discharges, leakages or spillages.
- Remediation Cost Cap: "Stop loss" programs designed to protect against cost overruns on contamination clean-up projects.
- Contractor's Pollution Liability: Coverage for pollution liabilities associated with contractor's operations, whether from the new incidents or the mobilisation of existing contamination.
- Combined Programs and Liability Buyouts: A blend of the principal coverages with a funded element to cover known remediation costs. Such programs can be structured to provide buyers and/or sellers with a long-term buy-out of environmental liabilities.

The Willis Index is a quarterly publication reporting on the relevant issues affecting the insurance industry and the impact they have upon our clients.

Our quarterly review will comment on and provide analysis of the environmental insurance market, assisting buyers and their advisors on available solutions.

In this our first issue, we provide a guide to environmental insurance, with answers to a selection of the questions we are commonly asked.

Regular features will include updates on the market conditions, case studies, technical analysis of coverage specifics and special features highlighting significant changes in regulation, insurance market news and forthcoming events and seminars.



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# Environmental Risk and Insurance – continued

## **What is the maximum period of insurance available?**

For a one-off premium payment, it is currently possible to obtain policy periods of up to ten years for historical contamination cover, and up to three or five years for "new" pollution cover. Combined programs and liability buyout programs offer the potential for longer policy periods.

## **Isn't this type of cover available through other policies?**

No. Traditional insurance products provide limited, if any, cover for pollution. At best, public liability policies may offer cover for third party claims arising from "sudden and accidental" pollution events, whilst property insurance may provide limited clean-up cover, but only if losses occur as a result of an "insured peril". Such policies are therefore clearly inappropriate for the majority of environmental risks, particularly those associated with historic contamination which is often the key concern during transactions.

Consultant's professional indemnity (PI) insurance solely provides cover for losses arising from the consultant's negligence, and is not therefore a substitute for environmental insurance. Environmental insurance can also be used to underpin or replace warranties and indemnities, or ring-fence liabilities incurred via such agreements.

## **How much does environmental insurance cost?**

Premium levels will depend on factors such as the limit of cover required, policy deductible (or 'excess'), policy period and, of course, the nature of the risk. The environmental insurance market is currently very competitive, with premium levels often starting at less than £15,000.

## **How long does it take to obtain environmental insurance?**

If necessary, environmental insurance can be procured within a matter of days. Even complex risks, requiring the review of substantial quantities of technical information, are routinely placed by Willis within transaction timescales.

## **What information is needed to obtain environmental insurance?**

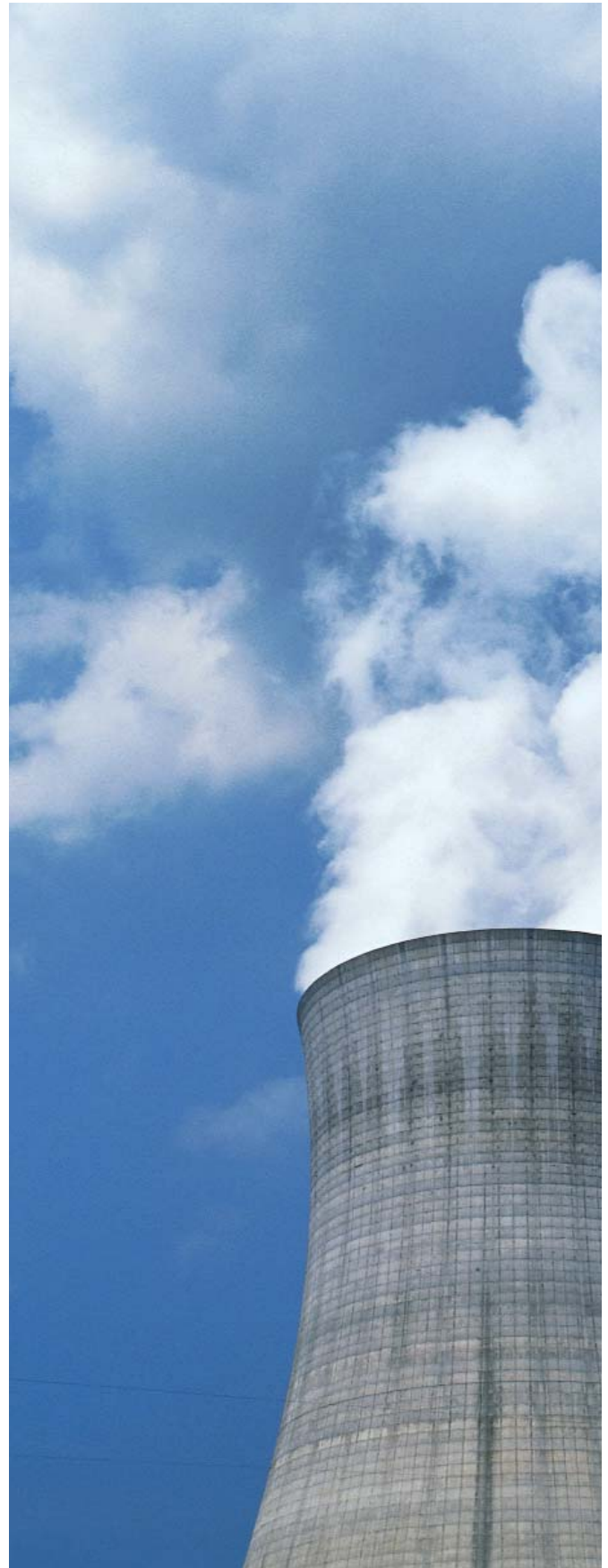
Typical requirements include desk study information (e.g. environmental database reports or 'Phase 1' reports), where necessary supplemented by 'Phase 2' intrusive investigations (e.g. at industrial sites with a long industrial history).

## **What happens if the insured property or company is sold?**

Environmental insurers are typically willing to assign policies or include additional insureds upon transfer of the relevant assets or business to a new owner.

## **Why is it important to use a specialist broker such as Willis?**

There is simply no such thing as an "off the shelf" environmental insurance policy, as they require careful scrutiny, evaluation and negotiation with insurers to ensure that the policy terms and conditions meet the client's requirements. As a market leading broker in this specialist field, Willis is ideally placed to deliver innovative, robust and cost effective environmental insurance solutions, often working in conjunction with environmental consultants and legal advisers.



# Focus On...

Environmental insurance has proven effective as a risk transfer mechanisms in a wide variety of applications. The environmental team at Willis have been successful at developing environmental insurance solutions for a wide range of applications. In this Willis Index, we focus on two common examples of Private Finance Initiative (PFI) contracts.

## Corporate Transaction

The allocation of environmental liabilities can become a significant point of contention between transaction counterparts, potentially jeopardising corporate and property transactions. By transferring such liabilities, environmental insurance can remove the issue from negotiations, enabling both buyer and seller to maximise value from the transaction.

A US corporation was concerned that it might inherit significant environmental liabilities following the share purchase of a UK target company. Previous investigations had identified soil and groundwater contamination beneath one of the company's sites, as a result of historic landfilling as well as manufacturing activities. Further investigations commissioned by the purchaser confirmed that remedial works were needed in order to mitigate risks to an adjacent watercourse.

By working closely with the preferred insurer, our client and their environmental consultants, Willis succeeded in placing insurance to cover the 'known' pollution as well as the unknown. Full cover was achieved by applying an increased self-insured retention to the known pollution until the remedial works had been completed.

This flexible approach enabled the deal to proceed within the required tight timescale, and allowed the purchaser to fix its maximum future exposure to environmental liabilities and factor this into the negotiations.



## PFI Projects

Willis have been environmental insurance advisers for both public and private clients in a range of PFI projects in housing, waste and construction related projects in UK and wider EU countries.

### Project Aquatrine

Project Aquatrine is a water and waste-water scheme across the UK Ministry of Defence (MOD) properties around the British Isles.

Under the contracts, the MoD transfer the responsibility and risk for the operation and maintenance of the MoD's UK water and waste water assets and infrastructure to private service providers. The assets and associated infrastructure are located in more than 3,000 UK sites which vary between large military establishments including; naval bases and former airports, firing ranges, residential estates and cadet huts. This diversity of sites presents a range of potential environmental liabilities related to both historic and operational risks.

Along with the ongoing operation and maintenance, the service provider also assumes responsibility for any future environmental liabilities which may arise from the historic operation of the water and waste water assets and infrastructure. The project agreement lays down a requirement to underpin this contractual apportionment of liabilities through the use of environmental insurance to a wide-ranging specification.

Willis advised and placed environmental insurance for one of the service providers awarded an Aquatrine contract, Willis was at the forefront of the development of a bespoke policy wording which completely overhauled the approach that had been previously applied to similar projects. The resulting insurance solution provided the service provider with long-term protection which not only satisfied the contractual requirements, but also benefited from a significant saving to the premium levels initially budgeted for environmental insurance.



Artists impression of the "Willis Building" currently under construction in the City of London, due for completion late 2007.

## Breaking News

The Willis Environmental Review is now available. Our review provides insurance buyers, professional advisers, financiers and other interested parties with a unique and invaluable insight into the current state of the global environmental insurance market, including the following:

- an update on market conditions
- an overview of recent product developments
- an insight into how these products are being applied
- a review of developing trends.

Much has changed in the environmental insurance market since our last review in 2002. Insurers have continued to build on the successful foundations laid down during the late 1990s, by broadening the market offering in line with clients' requirements.

Although the UK market remains small compared to its North American counterpart, it is now host to more environmental insurers than at any time, and a steadily increasing portfolio of specialist risk transfer products that can be tailored to individual requirements.

The next Willis Index will include extracts of the review, however in the meantime please contact us if you would like a copy, or visit [www.willis.com/environmental](http://www.willis.com/environmental) to download a copy.

Willis has won the Reactions Award for Insurance Broker of the Year and Most Innovative Broker of the Year 2005. The awards are voted for by the readers of Reactions and are open to all industry participants.

## Meet the Team



### David Barr MSc, BSc, FGS

#### Project Director – Environmental

David joined Willis in 2004 after gaining some 13 years experience in the petroleum industry and with an environmental consultancy. For much of this period David specialised in the provision of environmental due diligence, risk assessment and financial modelling services to the property and corporate sectors. David's technical and practical knowledge of environmental risk management has further enhanced Willis' capabilities in delivering innovative and bespoke solutions to environmental liabilities.

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## Did You Know?

### Cover for "Known" contamination

One of the many misconceptions about environmental insurance is that you cannot obtain cover for contamination already present at the proposed site i.e. "known" contamination. Time and again our experience combined with our knowledge of the approaches of key insurers has shown this to be far from the truth. A recent Willis example clearly illustrates this.

A UK property company was concerned that ground contamination issues at one of its properties could present significant future liabilities. The premises, now the site of a prestigious leased office development, had previously formed part of a major gasworks facility.

Although remedial works had been undertaken in the mid 1990s to the satisfaction of the planning authority, these works would almost certainly not have met current remediation standards.

It was evident that residual tars and contaminated groundwater had been left beneath the site, potentially requiring further clean-up to satisfy environmental regulators in the future.

Willis succeeded in placing environmental insurance to cover the current owner for a period of ten years, even in the event that they undertook minor development works or ground investigations at the site. In addition the policy included an option to continue extending the policy annually beyond the initial ten years.

Through the use of insurance, the owner gained comfort that the costs of any future additional clean-up as a result of increasingly stringent legislation or third party action would be met. In addition, the broad coverage negotiated by Willis would be attractive to a potential purchaser and thus help maximise the property value during future sale negotiations.

Willis is one of the World's leading risk management and insurance intermediaries. We have 15,800 professionals in over 300 offices around the World.

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