

## FINANCIAL ASSURANCE MANDATES EXPAND GLOBALLY

**A rising bar for environmental protection is meeting a rising bar for financial responsibility - and one result is expanding financial assurance mandates. Financial Assurance (FA) mandates require certain regulated entities to demonstrate that they have adequate financial resources to cover future liabilities, including such obligations as reclamation expenses following the closure of a mine or waste facility.**

As the prevailing economic conditions continue to negatively impact corporate balance sheets, many companies are struggling to find cost-effective ways to comply with FA requirements. Furthermore, we are seeing a global increase in the implementation and enforcement of FA provisions, and as a result, many companies are looking for solutions for the first time. In the U.S., a recent federal court ruling (*Sierra Club v. Johnson et. al.*) looks likely to accelerate FA requirements for companies involved in a much wider range of activities.

FA provisions are incorporated into local environmental legal frameworks across the globe. In the U.S., FA regulations have been a requirement for years for certain industry segments with a high polluting potential, for example, waste management facilities regulated under the Resource Conservation and Recovery Act (RCRA), certain mining operations and facilities with underground storage tanks. However, until now, other industry sectors with environmental cleanup obligations and related long-term liabilities have largely escaped the FA burden. As a result, corporate bankruptcies have left states, and ultimately taxpayers, footing the bill for environmental remediation and reclamation.



The U.S. Congress acknowledged this issue in 1980 when it enacted the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA, also known as the Superfund law). CERCLA required that facilities involved with hazardous substances be held financially responsible for cleaning up any improperly disposed of substances. However, for more than 25 years, the U.S. Environmental Protection Agency (EPA) has never fully implemented the CERCLA authorized requirements. The Government Accountability Office (GAO) and public interest groups have been actively pushing EPA to address this issue, and the recent court ruling now specifically mandates EPA to take action.



Many industry sectors will likely be affected by these new provisions, including power generators, chemical manufacturing facilities and metal finishers. Companies involved in mining operations may become a major target, since the EPA has ranked the mining industry as the highest priority polluter in the U.S.

Similar activity is taking place in other territories. In Europe, the European Liability Directive (ELD) requires member states to encourage the development of FA mechanisms. The EU Commission is required to present a report by April 2010 on the ELD's effectiveness, including the availability of insurance and other types of financial security for certain industrial activities. Depending on the outcome of the review, the commission may submit proposals for harmonized mandatory FA requirements across the EU.

Typically, FA regulations allow for a variety of compliance mechanisms, including corporate guarantees, trust funds, surety bonds, letters of credit and insurance. Each approach has different advantages and disadvantages that depend on the unique circumstances of the individual organisation.

Insurance has traditionally been a very competitive FA option and the environmental insurance industry has historically played an important role in providing a method to satisfy FA requirements. In many situations insurance offers a comparatively low-cost solution while providing additional advantages, such as true risk transfer protection.

## **NEW COMPULSORY ENVIRONMENTAL INSURANCE SCHEMES**

A number of countries have recently introduced compulsory environmental insurance programs designed to ensure that companies have adequate financial resources to address their environmental liabilities and obligations.

### **CHINA**

Earlier this year, China's national environmental regulator, the Ministry of Environmental Protection (MEP), announced the introduction of the Green Insurance System, a compulsory program that is expected to apply to all industries with high polluting potential. Combined with the recent introduction of the nation's Green Credits program, the new system marks a shift from regulatory enforcement to market instruments as the key tool for combating environmental problems.

The new environmental insurance system will be implemented in phases, starting with the industries at highest risk (e.g., the chemical and hazardous waste sectors). It is expected to take full effect by 2015.



## ARGENTINA

Toward the end of 2008, Argentina's government enacted a law requiring any company performing an activity that might pose a threat to the environment to provide evidence of insurance or financial assurance that would guarantee the financing of future required cleanups.

Although the law does not specify fines or penalties, government authorities will not renew operator permits for companies failing to comply with the insurance requirements, rendering those companies unable to operate legally in the country.

## EUROPE

The European Union enacted the Environmental Liability Directive (ELD) in 2007. While the directive does not demand compulsory environmental insurance for operators, it does require member states to encourage the development of appropriate financial security instruments and markets.

Some member states, when implementing the directive, have made Environmental Liability insurance or FA compulsory for operators, or are considering doing so. For example, Spain has mandated that certain industrial operators must buy environmental insurance or provide alternative financial assurance by April 2010 in order to obtain permits for conducting potentially polluting activities.

The international environmental insurance marketplace offers a variety of options for buyers to choose from. Multinationals with operations in China and Argentina should be aware that since non-admitted coverage is prohibited in both territories, evidence of local insurance is required.

## THE EU'S ELD - A WORK IN PROGRESS

Agreed in 2004 and adopted in 2007, the EU's Environmental Liability Directive (ELD) remains – by design – a work in progress. The directive goes beyond most national environmental protection

legislation, creating a liability framework designed to ensure that industrial operators are financially responsible for the damage they cause to the environment. At the same time, the ELD leaves the implementation of some issues to the member states' discretion, e.g., scope of liability, legal defenses available, scope of habitats covered and financial security provisions.

In most member states, laws empower authorities to pursue polluters in cases of water or soil pollution. Only a few member states (e.g., Sweden and Denmark) have enacted a more forceful regime dealing with compensation for damage to the environment. Under the ELD, operators are required to not only remediate environmental damage, but to take preventative steps to avoid damage in the first place, and in certain circumstances, pay compensatory damages. Other clear ELD requirements include:

- Strict liability for certain specific industrial and agricultural activities
- Fault-based liability for all other activities
- Provisions for prevention and compensatory remediation

Given the directive's flexibility, the pace of implementation has understandably varied across the EU. For example, the U.K. was one of the last member states to complete its ELD implementation. The necessary regulations became law in England on March 1, 2009 and will be followed by similar regulations in Wales, Scotland and Northern Ireland.

Unsurprisingly, companies are often unsure if their current insurance programs will provide effective protection against the new liabilities

created by the ELD. While the answer will depend on the specifics of each organization's insurance arrangements – and to some degree the country involved – here are some issues to consider.

A 2006 court decision in the U.K. (*Bartoline vs. Royal Sun Alliance*) determined that claims by regulators to recover cleanup costs were not covered under the insured's liability policy. Based on this ruling, it is unlikely that the costs associated with the ELD will be considered as "damages" or "compensation" and therefore would not be covered under a U.K. Public/General Liability policy.

Some European Casualty insurers now offer Pollution Cleanup extensions targeted at some of the exposures created by the ELD and covering certain cleanup costs mandated by authorities. However, while these extensions may offer some valuable protection, they are unlikely to cover the sort of costs associated with preventative measures or preliminary, complimentary or compensatory remediation obligations created by the ELD. In addition, cover under the Pollution Cleanup extensions are usually limited to off-site, sudden and accidental pollution, whereas the ELD could apply to gradual pollution and on-site pollution.

The specialist environmental market can provide much more comprehensive pollution coverage, including many of the exposures created by the ELD. Most importantly, coverage is not typically limited to off-site, sudden and accidental pollution, and can include gradual pollution and other forms of damage to the environment as well as on-site risks.

## JOINING OUR TEAM

### **Kelley George** **North America, Western Region (Los Angeles)**

Kelley is an environmental consultant with more than 18 years' experience in the environmental and insurance industries, as well as a strong background in legislative and regulatory processes. As an environmental consultant she has consulted on large projects for the military, state and local governments, and industry clients. She has also successfully underwritten and placed hundreds of millions of dollars in environmental insurance products. Kelley has more than 20 years' experience with environmental liabilities. She has worked as a researcher at HUBBS Institute of Oceanography and as an environmental consultant with Ogden Environmental and Energy services. She is also an experienced underwriter, and as a national accounts underwriter for AIG she underwrote complex environmental risk transfer mechanisms for national corporations, cities and the military.

## **Keith Jurss** **North America, Central Regions (Chicago)**

Keith is responsible for the environmental team supporting the Midwest and South Central Willis HRH regions. He is based in the Willis HRH Chicago office. In more than 20 years of broking and underwriting specialty lines of insurance coverage, Keith has worked extensively in the Environmental, Professional Liability, Transportation and Products Liability areas. He joined the Willis Environmental Practice from another major broker. He adds strength to Willis' market-leading capability in some key product areas, including Remediation Cost-Cap and Liability Transfer programs.

## **Clive Walker** **Europe, U.K. (London)**

Based in London, Clive is responsible for broking and developing environmental insurance products throughout the U.K. and Europe. He has more than 11 years' experience as an environmental risk management specialist. Prior to joining Willis in 2008, he held a senior position in the M&A team of a leading environmental consultancy, where his responsibilities included project direction of global multi-site due diligence projects and U.K. business development.

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