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A GUIDE TO THE

ENVIRONMENTAL LIABILITY DIRECTIVE

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A GREENER BUT MORE LITIGIOUS FUTURE

Welcome to this guide on the Environmental Liability Directive. Now transposed into the legislation of most of the EU member states, the ELD has potential implications for many European companies.

While the directive holds fast to the now established EU rule of 'the polluter pays', there are many uncertainties surrounding this new legislation. It tackles the hitherto unexplored area of the effects of damage on wildlife and habitats – a loss which is incredibly difficult to quantify, particularly as polluters may be required to 'make good' on another site. It requires operators to take preventative actions where their activities pose an 'imminent threat' of environmental damage – once again, a hard issue to assess.

There is no doubt that it will take some years for the imponderables to be resolved. And this resolution will no doubt be through some expensive legal battles with the authorities involved.

We have produced this guide to help European companies tread safely through this particular minefield – without producing any environmental damage on the way!

Sue Copeman
Editor, StrategicRISK

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FOREWORD

The Environmental Liability Directive will have wide ranging implications for companies throughout the EU, explains Simon White

The sinking of the oil tanker Erika in 1999 was seen by many as a milestone in setting Europe on course for tougher environmental laws. The Erika went down in the sea off Brittany spilling thousands of tons of oil when she broke up. Over 400 kilometres of French coastline were destroyed by crude oil, killing tens of thousands of birds.

The public outrage following the disaster helped establish the belief in the eyes of the politicians and the general public that polluters should pay compensation to those impacted by their actions. In this case the oil giant Total, who had chartered the Erika, not only ended up paying more than €200m towards an extensive cleanup operation but, in a landmark ruling, was fined a further €375,000 for the ecological loss 'resulting from the damage caused to the environment'. The judge ruled that Total should compensate nearly 100 parties impacted by the pollution including fishermen, hoteliers and bird protection associations.

The European Environmental Liability Directive is another milestone, strengthening the 'polluter pays' principle even further. Earlier this year, nearly a decade after the sinking of the Erika, this key directive was transposed into law in England and Wales. While there has been a rising interest by UK firms in the directive, some are relying on their existing procedures and hoping they are not affected or believing this law is not relevant for their company.

However, it is clear that the way companies deal with a pollution incident will need to change. Under the directive, for instance, polluters are required to take immediate steps to prevent damage to the environment and, perhaps more importantly, to notify the enforcing authority of a potential incident. Non-compliance could in the worst case lead to a criminal prosecution, a risk no company director would want to face. This requirement alone is expected to increase the number of notifications to the regulator, something we have already witnessed in EU countries which have implemented the directive over the last two years.

The directive also requires authorities to enforce the 'polluter pays' principle, requiring a cleanup and possible compensation for the environment.

Key changes for companies as a result of the ELD are:

- Certain natural habitats and species are protected by having their own legal rights and, if damaged, there may be a requirement for compensation to the regulator in the form of a material action or financial payment (compensatory remediation)
- 'Complementary remediation' may be required if the polluted area cannot be brought back to its baseline condition following a cleanup. This could, for instance, involve acquiring new land and creating a complementary habitat from scratch.

Wide remit

In relation to the special natural habitats requiring protection, the UK like some of the other member states has gone beyond the so-called 'Natura 2000' sites. In England this also includes around 4000 sites of special scientific interest (SSSI). It is therefore likely that many companies operate in relatively close proximity to one of these specially protected natural habitats.

Importantly the directive not only deals with pollution incidents, but also damage caused to the environment. Companies could, for example, be held liable for causing damage by flooding an SSSI even if the water as such was not polluted.

Local community groups and NGOs also have the right to ask the authorities to investigate potential polluters should they feel the initial response by the authorities was inadequate. In countries which have implemented the ELD, we have seen NGOs making use of this right and expect similar action in the UK, with its long history of local pressure groups.

Getting the right cover

Some firms still believe that their public liability (PL) policies cover a significant proportion of their environmental risk. However, since the 1990s, PL policies have been generally restricted to sudden and accidental events, still leaving some confusion as to what, in terms of environmental liabilities, the PL form does cover. In most cases the PL policy will not respond to a gradual pollution condition or first party cleanup of soil and groundwater. In addition, there is considerable uncertainty as to whether such policies would respond to statutory liabilities following intervention by an environmental regulator where there had been no claim by a third party, for example, the pollution of groundwater resulting in a cleanup notice from an environmental agency.

Environmental claims are notoriously complex and expensive and it may take some time before the full costs of claims under this relatively new directive come to light. The EU encourages the uptake of a form of financial provision to pay for the expected increase in cost of the environmental claims under the directive. A few member states are even making financial provisions for claims mandatory, something that it is anticipated will be reviewed on an EU-wide basis over the new few years.

Reuters

The stern section of the oil tanker Erika points skyward as it flounders in heavy seas off the coast of Brittany. The broken tanker finally sank while it was being towed further out to sea.

Insurance is an obvious way of ensuring the right financial provisions are in place and a strong specialist environmental insurance market has developed providing cover for all liabilities under the ELD. Environmental policies combine third party liability and first party property coverage, and include on- and off-site cleanup costs, and legal defence and technical expenses for sudden and gradual pollution conditions.

Many agree that the ELD will have wide-ranging implications for companies throughout the EU. I hope you find the information in this guide to the ELD useful and after reading I am sure you will agree that the ELD is too important to be ignored.

Simon White is environmental branch manager of XL Insurance

EUROPEAN OVERVIEW

Pierre Sonigo gives his own perspective on the development and complexities of the ELD

As early as 1993, during discussions on the Green paper of what was to become the Environment Liability Directive, and then in 2000 when the White paper was prepared, industry representatives expressed concerns about the new liabilities this regulation would imply. Although agreeing with the environmental objectives of the directive, they were concerned about the potential financial impact of unknown applications of this new legislation. They therefore insisted that these new risks be mitigated and that adequate insurance coverage be available to protect them. The legislator listened and required that specific insurance products be developed in that respect. More than 10 years later where do we stand?

Clearly, three issues remain pending from a risk manager's perspective: the legal imbroglio of the transposition of the directive in the 27 countries of the EU, the difficulty in analysing the adequacy of insurance solutions available for the new exposures resulting from the directive, and the lack of tools to do a proper risk assessment to determine if insurance is needed in the first place.

The framework directive left a wide margin for the implementation of important measures at the discretion of the member states. This applies to the scope of liabilities, the exemptions granted (permit to operate and state of the art), defences, etc. The directive only represents minimum requirements, and each member state can adopt more stringent provisions if they wish. A few of them did not hold back from doing so!

Twenty member states have notified complete transposition of the directive but seven received condemnation from the Court of Justice for not having done so (Austria, Finland, France, Greece, Luxembourg, Slovenia and the UK).

Some member states decided to update existing laws to accommodate the directive; others took this opportunity to clean up their regulations and replace old texts with new ones, but a few decided to keep the old ones and just add another layer of regulation, which can only make the system more complex to implement. All this can make the job of a risk manager who wants to establish a European cover (including the possibility of cross border events) for his entities an almost impossible task.

Today many insurance products claiming to cover the new risks generated by the directive exist in the market. Some are offered by private insurers, other by pools. In six member states (Bulgaria, Czech Republic, Greece, Hungary, Portugal, Romania, Slovakia, Slovenia and Spain), the coverage is even compulsory by law!

The problem is that a detailed analysis of the wording of some of these contracts shows that not all potential consequences are covered. Many doubts remain on the applicability of the policy and the claims handling. Such factors as the policy trigger, the applicable law (civil or public), the definition of environmental damage, the types of indemnification (preventive and remedial actions), the temporal limitations to name a few, are handled differently in each coverage and are not always clear.

The debate whether coverage needed for the ELD should be an extension of existing

liability policies (general, automobile, marine, professional, D&O) or should be written in separate contracts is not over yet. After all, many insureds consider that they already have adequate pollution insurance for sudden and accidental events which cover traditional damage (bodily injury, property damage or economic loss). Why not just extend them to water, soil natural habitat and endangered species? The directive requires a 'restoration in kind' which means an obligation to restore, rehabilitate or replace damaged natural resources/services, or to provide an equivalent alternative to these resources.

It is no wonder that industry representatives and their insurers (possibly also the competent authorities in charge of the implementation) are not very comfortable with these new concepts!

Despite the new policies they have developed, insurers complain that industrial buyers are not keen on purchasing the coverage. The reasons are obscure: is it the lack of clear understanding of the specificities of the directive? the silos existing between environment experts and insurance managers in many companies? or simply a poor appreciation of the risk exposures?

It is true that doing a proper risk assessment of real exposures is not very easy. The directive normally applies to Natura 2000 areas. Often there is little or no knowledge of the natural resources around production facilities. It is also important to determine and monitor over time the 'baseline' of natural habitat and endangered species to be used as a reference after a loss. Clearly adequate expertise is lacking in these areas. All this means that large amounts of money will be spent in consultants' and lawyers' fees before and after a loss to assess pre-existing conditions, preventive measures and the environmental damage, determine remedial actions and negotiate with the competent authorities acceptable solutions, or litigate to come to a reasonable agreement.

There is not sufficient loss information to use a sound statistical base for projecting what the future will look like

There is not sufficient loss information to use a sound statistical base for projecting what the future will look like.

The Commission has to report before 30 April 2010 on the effectiveness of the ELD in terms of actual remediation of environmental damage, and the availability at reasonable costs and conditions (whatever that means) of insurance and other type of financial guarantees for the activities listed in Annex 3 of the directive.

It will be difficult for this report to reflect the complexity of the existing situation. Let us hope for a balanced document which will allow flexibility to solve the remaining challenges still ahead.

Pierre Sonigo is secretary general of the Federation of European Risk Management Associations

APPROACHES IN EUROPE

Andrew Williams looks at the approaches some major EU states have taken in transposing the ELD into national law

Directive 2004/35/EC on environmental liability with regard to the prevention and remedying of environmental damage, commonly known as the Environmental Liability Directive (ELD), introduces the concept of 'polluter pays', under which identified companies must bear the cost of rectifying environmental damage to soil, water, protected species or protected habitats and take measures to prevent it resulting from their operations.

This article investigates progress towards transposing the ELD into national law in five of the largest EU member states, France, Germany, Italy, Spain and the United Kingdom. In doing so, it highlights some of the main characteristics of each law and seeks to provide a brief sense of the individual approach towards the design and delivery of environmental regulation in each country. Where appropriate, it also highlights any major environmental incidents that may have inspired that approach.

Main features of the directive

The directive's principal aim is to hold businesses financially liable for environmental damage caused by their activities, which should result in an increased level of prevention and more precautionary measures. Moreover, the ELD requires operators to take preventative actions where their activities pose an 'imminent threat' of environmental damage (ie where there exists 'a sufficient likelihood that environmental damage will occur in the future').

The ELD employs two distinct but complementary liability regimes. Firstly, there is a strict liability-based regime that applies to operators carrying out hazardous activities as set out in Annex III and secondly, a fault-based regime that applies to all other business activities.

Wherever operators are found liable under the ELD, they are required to undertake a range of 'remedial measures' (see Table 1), defined as 'any action or combination of actions, including mitigating or interim measures to restore, rehabilitate, or replace damaged natural resources and/or impaired services or to provide an equivalent alternative to those resources or services as foreseen in Annex II.'

Most EU member states have now enacted the directive

The transposition process

The ELD is a Framework Directive, and as such it leaves significant discretion to the member states in several important areas, including the allowance of state of the art and permit defences, the definition of biodiversity, scope, causation, financial security and the extent of operator liability, thus enabling stricter or weaker measures to exist from one member state to another.

Although transposition of the ELD and the drafting of legislation is still ongoing in some countries after the deadline of 30 April 2007, most EU member states have now enacted the directive. As of April 2009, only seven countries, (Austria, Finland, France, Greece, Luxembourg, Slovenia and parts of

Table 1 - Overview of remedial measures provided for in ELD	
Type of Measure	**Description**
Primary remediation	Any remedial measure that returns the damaged natural resources and/or impaired services to, or towards, baseline condition
Complementary remediation	Any remedial measure taken in relation to natural resources and/or services to compensate for the fact that primary remediation does not result in fully restoring the damaged natural resources and/or services.
Compensatory remediation	Any action taken to compensate for interim losses of natural resources and/or services that occur from the date of damage occurring until primary remediation has achieved its full effect. Interim losses are defined as 'losses that result from the fact that damaged natural resources and/or services are not able to perform their ecological functions or provide services to other natural resources or to the public until the primary and complementary remedial measures have taken effect. It does not consist of financial compensation to members of the public.'

the UK), have not finalised the transposition, although in most cases government bills or similar draft legislation has been or is being discussed and is expected to be adopted shortly.

In general, insurance is the most popular instrument to cover environmental liability, followed by bank guarantees (Spain and UK) and market-based instruments (Spain).

France

In July 2003, the French Parliament established an environmental act, which laid the foundation for all future environmental regulation in the country. The act formally codified the 'rights' of the environment as enshrined in four overarching principles: the precautionary principle, the preventative principle, the principle of participation and the 'polluter pays' principle.

The adoption of the new environmental code meant that much of the necessary groundwork for the establishment of a national law of environmental liability had already been undertaken well in advance of the ELD transposition deadline. Even so, it was not until August 2008 that France finally adopted Law number 2008-757 '*relative à la responsibilité environnementale et à diverses dispositions d'adaptation au droit communautaire dans la domaine de l'environnement*', which was the first step towards implementation of the ELD in the country. However, the nature of the domestic French legal process means that the adoption of a décret (decree) is still necessary for a complete transposition. This is not currently expected until the end of June 2009.

The French ELD legislation does not allow permit exemptions, but does include a provision allowing operators to apply for a 'state of the art' exemption. Moreover, France has not decided to enforce compulsory financial security and has adopted fault-based liability for environmental damage to protected ➤

Rex

Environmental workers clear dead fish from the River Rhine after a fire at Sandoz chemical plant released poisonous mercury into the waterway.

species and habitats caused by 'non-Annex III activities.' In those cases of environmental damage caused by more than one operator, the national law applies liability on a proportional basis on the basis of the views of the competent authority.

Germany

More than 20 years ago, a major environmental incident in the River Rhine sparked the beginning of the legal debate on environmental liability in the EU. In 1986, a major chemical leak at the Sandoz warehouse in Basel, Switzerland led to massive mercury pollution and the death of half a million fish throughout the river basin. In direct response to this ecological disaster, the European Parliament and Council of Ministers issued a resolution requesting the Commission to propose a regulation imposing civil liability for environmental damage to Rhine and other main transportation routes in the EU, a key precursor to the ELD.

On 14 November 2007 the German '*Gesetz zur Umsetzung der Richtlinie des Europäischen Parlaments und des Rates über die Umwelthaftung zur Vermeidung und Sanierung von Umweltschäden*' (known, for short as the '*Umweltschadensgesetz*' or 'Environmental Damage Act') came into force, formally transposing the ELD in the country.

A key feature of the German legal system is that any of the 16 German Bundesländer has the power to modify the existing federal rules individually at the regional level through implementing provisions. So far there are no expected differences between the regions.

Exemptions, whether based on 'permit' or 'state of the art' defences, are not allowed in the federal legislation. Furthermore, joint and several liability applies in cases of envi-

ronmental damage caused by more than one operator, with fault-based liability attached to environmental damage caused by 'non-Annex III activities' and strict liability for damage caused by genetically modified organisms (GMOs). The German act does not impose compulsory insurance or any other financial security on operators. However, it does apply retrospective liability for environmental damage caused from 30 April 2007 onward.

Italy

Legislation aimed at the prevention and control of accidents involving dangerous substances in the EU was significantly prompted by one notorious disaster in Italy's past. In 1976, a chemical plant manufacturing pesticides and herbicides in Seveso, Italy accidentally released large amounts of poisonous dioxins into the air, contaminating 10 square miles of land and vegetation. Over 600 people were evacuated with as many as 2,000 treated for dioxin poisoning. As a result, in 1982, the Seveso Directive (Council Directive 82/501/EEC) on the major accident hazards of certain industrial activities was adopted.

In Italy, liability for environmental damages extends beyond the scope of the directive

In 2006, Italy adopted legislation that formally transposed the ELD into national law, becoming the first of the 'major' EU countries to do so. The Environmental Code-Legislative Decree No 152 of 3 April 2006 includes no measures on compulsory financial security but does allow state of the art and permit exemptions. Fault-based liability applies for cases of environmental damage occurring as a result of non Annex III activities, with proportional liability attached to cases caused by more than one operator.

The domestic law also enforces protection to a significantly wider range of species and natural habitats than required by the ELD, meaning that, in Italy, liability for environmental damages extends beyond the scope of the directive.

Spain

On 25 April 1998, a tailing dam break at the Boliden mine near Aznalcóllar in southern Spain led to one of the most harmful environmental incidents in the history of the country. The rupture released around five million cubic metres of toxic tailings slurries and liquid, containing lethal levels of heavy metals. The accident devastated the local environment, contaminating a 40 km stretch of the Agrio and Guadiama rivers as well as vast swathes of surrounding farmland.

In total, almost 40 tonnes of fish and around 100 vertebrates were killed, with approximately 5,000 geese and 20,000 water birds also seriously affected. Remedial activities required the excavation of 12m tonnes of contaminated soil and resulted in a total economic loss in the region of €400m.

The disaster was particularly damaging because the Doñana National Park is one of Europe's most important natural sites. It was declared a World Heritage site by UNESCO because of its unique eco-diversity, consisting of lagoons, marshlands, dunes, and scrub woodlands. It is also an important resting place for migratory birds and the accident occurred in the middle of the bird-nesting season, which meant an increased risk for the bird population. Furthermore, the high concentration of toxic metals posed an alarming threat to the human population and the ecosystem.

It is perhaps partly because the Boliden ➤

incident still looms so large in the Spanish collective memory that, of the five countries analysed here, Spain has adopted the most stringent approach to the transposition of the ELD.

On 23 March 2007, Spain fully transposed the ELD into domestic legislation through Law 26/2007 – The Environmental Liability Act. As well as applying to species and habitats in Natura 2000 areas' soil and water (as required by the directive), the law also extends the scope of protected habitats and species to include all flora and fauna species covered under national and regional law, as well as the entire Spanish coastline

Spain has also adopted controversial (at least initially) provisions on mandatory financial security, not necessarily restricted to insurance products. Instead, operators may choose between different options including insurance, bank bonds and asset deposits. Financial guarantees will be compulsory by the end of April 2010, with the minimum amount to be determined by the competent authority according to the risk level and expected to range from a minimum of €300,000 up to a maximum of €20m.

In other measures, state of the art and permit exemptions are allowed, although the state of the art defence is limited to remediation costs only and not prevention costs. Furthermore, the operator must pay all costs in every case, but is entitled to recover remediation costs from the public administration.

A key difference between Spain and the other countries covered here is that fault-based liability exists not only for habitats and species, but for all categories of environmental damage. Where cases of environmental damage are caused by more than one operator proportional liability will apply, provided an appropriate share can be estimated.

Similarly to Germany, the Spanish law also applies retrospective liability for environmental damage caused from 30 April 2007 onward. Moreover, variations in legislation are possible at a regional level. However, no major differences are currently expected, with those that do occur likely to be mainly procedural in nature.

Millions of gallons of toxic water burst from a reservior at the Aznalcóllar mine and spilled into the river Guadiamar which feeds the Doñana wetlands, in southern Spain, killing fish and birds.

Rex

United Kingdom

In the UK, perhaps more than any other EU member state, the transposition of EU directives into domestic legislation is fraught with difficulties. The legislative history of the country has meant that each constituent nation of the union has evolved its own separate legal system, often rendering the adoption of a uniform 'UK-wide' law impossible.

Even so, after lengthy delays, Gibraltar, England and Wales have fully transposed the directive (in December 2008, February and April 2009 respectively). Scotland and Northern Ireland have still not fully transposed, but are expected to do so shortly.

In England, a regulation transposing the ELD (The Environmental Damage (Prevention and Remediation) Regulations 2009) took effect on 1 March this year. The scope of the English regulation is identical to the directive, with the addition of sites of special scientific interest (SSSIs) – extending strict liability to damage caused by non-Annex III activities to water, land, protected habitats and species. The extension of scope to include SSSIs is also in place in regulations in Wales and is anticipated in the forthcoming regulations in Scotland and Northern Ireland.

In common with most of the major EU countries (apart from Spain), the English (and, it is anticipated, other UK) regulations do not include any measures on compulsory financial security. Moreover, the permit and state of the art defences allowed under the directive have been adopted.

In English multi-party causation cases, liability will be 'joint and several' but operators are permitted to recover all or part of the costs from any other person who also caused the damage. The English regulation also stipulates that damage caused by an act of terrorism (but not of war) is excluded.

In England, there will be no liability for 'historic' pollution – since the implementing regulations exclude any damage that took place before 1 March 2009 as well as damage that takes place afterwards but is caused by an incident, event or emission that took place before 1 March 2009.

In Wales, operators will also be held liable for any environmental damage caused by genetically modified organisms (GMOs).

Conclusion

The adoption of the ELD will raise the standard of environmental protection across the EU and lend a welcome air of formality to an area of regulation that has previously been characterised by uncertainty.

The above analysis shows that, in some of the larger EU countries at least, the directive has now been largely implemented at the domestic level. It also highlights that some member states, notably Spain, have used the inherent flexibility in the ELD transposition process as a spur to adopting more stringent laws than they might have otherwise.

However, the process has not been without its critics. In particular, many practitioners in the risk industry have pointed out that the ELD's status as a Framework Directive has resulted in an overcomplicated system of national laws. According to a recent report on 'Navigating the Environmental Liability Directive' by the European insurance and reinsurance federation (CEA), 'The manner in which the ELD has been transposed means that there is no harmonised liability system. This means that there is a strong possibility that there will be variations in enforcement. These issues pose quite significant challenges for the insurance industry for both underwriting and claims. At European level there is now an absence of one of the most important prerequisites for insurability, ie legal clarity and certainty.'

Andrew Williams is a freelance writer

GREENING BUSINESS

How will the ELD work in practice? **Cliff Warman** gives some pointers

Over recent years, a number of regulatory requirements associated with reducing the environmental impact and ensuring the effective remediation of legacy environmental liabilities have been placed on businesses. With the implementation of the EU's Environmental Liability Directive (ELD), and its transposition into national legislation in each of the EU member states, comes a regulatory framework which requires a more responsible approach to environmental risk management. This is achieved through the prevention and mitigation of potential environmental damage and the concept of giving the environmental an inherent 'value' as a resource, in terms of scope of remediation required should environmental damage actually occur.

The Environmental Damage (Prevention and Remediation) Regulations (2009) in the UK defines how businesses will be required to take all practicable steps to prevent environmental damage without delay, where there perceived to be an imminent threat of significant damage, and how operational businesses will be held liable for any environmental damage actually caused. In addition, the concept of remediation has been extensively extended to include activities necessary to 'compensate' the environment for the damages that have been caused, either on a site basis or on a temporal basis, or both.

The main driver behind the concept of giving the environment and natural resources an inherent value by implementing such a regime is to promote the degree of responsibility that a business must take in potential environmental impacts and to ensure that the polluter pays. In addition, the 'precautionary' principle has been adopted to ensure environmental damage is prevented and mitigated wherever possible. These principles require that operators are fully aware of the risk they run, in terms of the potential for environmental damage to be caused, and to assess the potential scenarios that could lead to an imminent threat of environmental damage or to an actual environmental damage event.

A number of high impact environmental incidents have occurred over recent years, which would likely have been covered by the auspices of the new ELD should it have been in place at that time. However, due to the fact that the directive does not impose retrospective liability, the environmental damage caused did not infer such liability.

High impact incidents

Some of the highest profile environmental damage incidents are characterised by spillages of highly toxic chemicals to sensitive aquatic habitats, such as surface watercourses. One such spill occurred due to the run-off of chemicals into the River Rhine in 1986. The incident started with a fire at a pesticide and herbicide manufacturing plant in Switzerland, and as a result of the large volumes of water used to put out the fire, high concentrations of pollutants, with a high toxicity to flora and fauna, entered the river. The pollution migrated down the length of the river, across a number of national boundaries, killing entire populations of fish, with some species being completely eradicated. Preventative action in this case could have included the capacity to retain large volumes of surface run-off (fire-fighting water) on the site rather than

releasing to the river, an thus a highly proactive approach would have been required to anticipate the potential environmental damage that could be caused by a large scale fire at the site.

In a similar case of a fire at a chemicals storage and distribution site in the UK, the resulting pollution was caused again by fire water run-off, augmented by the impact of

Environmental liability is now a critical risk issue for many firms

fire-fighting foam entering a neighbouring river, and causing significant environmental damage to the natural habitat and the fauna. In this case the Environment Agency was mobilised to immediately undertake a degree of clean-up on the river. The Environment Agency latterly sought to reclaim the costs of the clean-up work from the chemicals company. It is understood that the scale of the on-site and off-site clean-up associated with this incident totalled several millions of pounds. When the chemicals company tried to claim the costs for clean-up of the river from their public liability insurer, on the understanding that the fire was a 'sudden and accidental' event and, as such, third party clean-up costs should be covered, the insurer in this case declined to pay. The reason for declining the claim was stated as being that the regulator's claim for statutory costs would not be defined as 'damages' to a third party, and as such was not covered.

In both of these cases, the environmental damage caused was due to a contingent risk associated with a primary damage event, ie a fire, and the resultant pollution was caused by the activities associated with the putting out of the fire.

The amount and extent of remediation likely to be required under the ELD in these types of environmental damage cases would likely include the rehabilitation of the environment which had been impacted. In the case of a highly dynamic habitat such as a river, it could be envisaged that both complementary remediation, and compensatory remediation would be required. For example, where a river that has been impacted cannot be cleaned up and rehabilitated to the extent that it is deemed to have returned to a 'baseline' condition, (ie the physical and ecological condition that existed before the damage occurred), then rehabilitation work at another, equivalent site would likely be required. In addition, where the remediation work on the impacted river would require many months or years of work to get the habitat back to the baseline status, compensatory work at another site or habitat would likely be required to compensate the environment.

It is clear that environmental liability is now a critical risk issue for many firms. The ELD has been structured to imply liabilities for companies that cause 'environmental damage', and not just companies that cause 'pollution'. It is therefore crucial that firms take into account potential issues associated with non-pollution related environmental damage, such as sediment run-off, or severe vibration that could cause environmental damage, without any requirement for a pollution event. Firms that fail to fully address their environmental risks do so at their peril.

Dr Cliff Warman is leader of the environmental practice in Europe, the Middle East and Africa at Marsh

BUYING THE RIGHT COVER

What should you look for if you need to transfer your potential ELD liability? **Simon Johnson** explains

The EU Environmental Liability Directive (2004/53/EC) (ELD) has created new risks and exposures to liability, in turn leading to new questions for companies to ask about their insurance and any environmental cover.

The ELD entered into force on 30 April 2004 and was implemented three years to the date later in 2007. In England and Wales, this took place on 1st March 2009 through the Environmental Damage (Prevention and Remediation) Regulations 2009.

The EU, in contemplating these regulations, aimed 'to establish a common framework for the prevention and remedying of environmental damage at a reasonable cost to society...' These regulations are therefore about protecting and restoring the environment in the event of future damage rather than dealing with historic or legacy issues, supporting the wider objective for sustainability.

Although the ELD builds on the polluter pays principle, it only talks about damage to land, water, and protected species and natural habitats.

Key points to note about the ELD are:

- The ELD is about damage, however it occurs. It includes pollution, but not exclusively resulting from pollution incidents. For example, a fire spreading outside the site boundaries to the neighbouring environment could lead to damage from emissions or from fire-water spreading contamination and residues affecting the environment, water and land.
- Pollution incidents that cause damage can be sudden and accidental, or gradual, or even a combination of the two; there is no distinction made.
- The operator is the principal liable person and that person can have strict liability where the operations fall within those described in Annex III of the ELD, including operations under integrated pollution and prevention control regime (IPPC), waste management, etc.
- The damages that are regulated are described in Annex II of the ELD.

With the exception of the first stage of any primary remediation, the rest of the damages and costs represent a new exposure for companies and operators across Europe. As yet, there are no proscriptive methods for calculating complementary and compensatory remediation. This creates significant uncertainty about the costs of any actions that will be required to be undertaken by the authority in regulating environmental damage and particularly damage to protected species and habitats.

Environmental insurance

It is unlikely that any standard public liability, general liability or property insurance programme will provide cover for any of the losses and damages under the ELD, except perhaps for some elements of primary remediation. Even then it depends on the policy providing cover for damages imposed by a regulator under regulation and not the legal claims for damage of a third party.

For those exposed to the risk of causing damage to the environment, who could be held liable, protection is available through the environmental insurance market. These markets, particularly over the last 12-18 months, have all expanded coverage to include losses and damages under the ELD or by any national legislation or country law implementing the ELD.

Are there any sub-limits for environmental damage or for the compensatory and complementary damage elements?

Important points to note and questions to ask, include:

- Are there any sub-limits for environmental damage or for the compensatory and complementary damage elements?
- How does the policy cover imminent threat of damage – part of the ELD process to prevent damage?
- What is the policy trigger for environmental damage? Is it a pollution trigger or is there a separate environmental damage trigger?
- Is it possible for the policy to recognise an April 2007 retroactive date, the date at which the EU wanted all member states to have transposed and implemented the ELD? While some transpositions clearly state that operators will only have liability for damage occurring after the transposition date in that country, ie for England 1 March 2009, others have back-dated transposition to April 2007.
- Can business interruption costs and losses be included?

Insurance is purchased to provide protection, create (financial) certainty and respond in the event of a claim. Although early days, claims are beginning to appear and from these first experiences it is possible to report that they are:

- complex – cause, damage assessment and actions
- require immediate response and expert claims handling
- need expert liaison/communication with:
  - o local enforcement agencies
  - o communities, and
  - o NGOs/pressure groups
- cost more than similar damage would before the ELD.

It is important that the insurer:

- has environmental underwriters
- can respond rapidly to complex environmental claims, and
- demonstrates a long-term commitment – claims may take decades!

In the future, environmental insurance may become a necessity if other countries and the EU follow Spain's example, where they are implementing a system of compulsory financial security in 2010. This security can be met by an appropriate environmental insurance policy. The EU is committed to ruling next April (2010) on whether to impose compulsory financial security on at least those with strict liability and potential substantial exposures. At present it is a voluntary arrangement only.

The ELD presents a liability and exposure to new types of damage across the EU. Operators are exposed and claims are already beginning to come through, so the risk is real. Unless a specific environmental insurance policy with coverage for these damages is part of the programme then full coverage is highly unlikely and companies risk a significant uninsured loss.

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QUESTIONS & ANSWERS

What new liabilities does the EU directive introduce?

Under various pieces of law, companies have always been responsible for the pollution they cause – the ELD just brings it all together, harmonising liabilities across member states to a minimum level.

But the potential impact is big. Previously, if a company caused, say, a fuel-tank leak into a local river, the regulator would clean it up and then bill the offending company for the remediation. Now, regulators have the power to demand additional improvements to damaged areas.

The legislation also makes the polluter responsible for reporting incidents to the regulator. And it encourages third parties to report pollution and compels the authorities to investigate every report they receive. As societal expectations that we live in a clean and green environment increase, penalties are only going to get tougher.

Until test cases hit the courts it is hard to say exactly what demands regulators will make or what kind of resources they will devote to investigations. In Spain there are several active claims, but they are still working their way through the legal system.

Worryingly, there are some signs that the liabilities could be huge. One of the biggest potential problems arises from a new approach to remediating environmental damage.

The ELD says that if a company causes damage to the environment it should take measures to return the environment to the condition it was in before the pollution occurred.

If the damage is irreversible, if, for example, a species has been wiped out altogether, the law says the polluter must 'make amends'. Exactly what constitutes making amends is not completely clear.

Additionally, as the directive uses the words 'environmental damage', not just pollution, operators could be responsible for damage caused by excessive noise or vibrations.

Will my public liability or property insurance cover me?

Companies usually expect their public liability or property cover to protect them in the event of pollution.

Since the early 1990s, however, public liability policies have limited cover to sudden and accidental pollution. And these policies pay out for damage to third-party property only.

Meanwhile, property policies only kick in when pollution results from an 'insured peril' such as fire or flood, and is sudden and accidental.

These policies may also exclude the removal of contaminated soil, which is unfortunate since most pollution claims arise when damage occurs gradually.

In such a case, the clean-up will often involve removing large amounts of contaminated soil at considerable expense.

Is the insurance market responding with new products?

In light of the Bartoline case, which demonstrated the limitations of public liability policies in the context of environmental damage, the insurance industry has begun to respond with specialist environmental insurance.

The industry has had to overcome challenges, because many of the new concepts are alien to insurers. They are also understandably reluctant to take on indefinite liabilities after their experiences with asbestos.

In some cases the regulations have demanded a response from the insurance industry. In certain parts of Europe, including Hungary, Croatia, Romania, Poland, Slovenia and Sweden, operators are required by law to have financial protection of some sort.

In May, the British Insurance Brokers' Association launched a environmental liability scheme in conjunction with Gallagher London. The scheme, underwritten by ACE European Group, provides brokers with an online premium quoting system for broad environmental cover, including first party clean-up costs and gradual pollution liability.

Meanwhile, Liberty International Underwriters Europe, a division of Liberty Mutual Group, launched a new environmental impairment liability unit to underwrite business.

XL Insurance also boosted environmental coverage under its general liability policies issued in the UK. The clean-up costs and Environmental Liability Directive endorsement provides cover for up to £1m against environmental liabilities including on and offsite clean-up costs for gradual as well as sudden and accidental pollution events for operations within the EU.

What steps should I be taking to prevent environmental damage?

Operators can reduce the likelihood of ever being caught by the regulations by minimising the risks to natural resources.

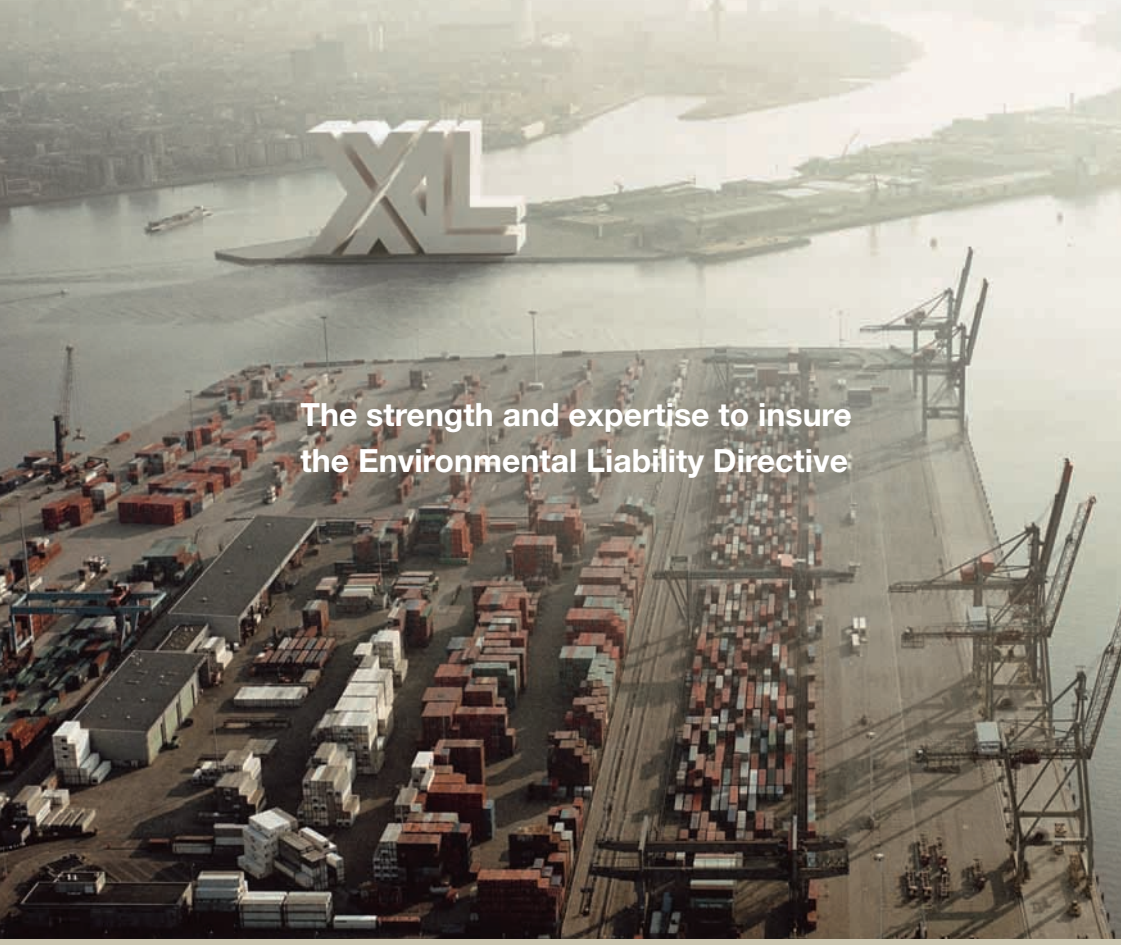
Strategies should cover damage to species and habitats, water and risks to human health from contamination of land. But any environmental damage may be relevant if it significantly impacts humans or has adverse effects on the environment.

Companies may want to consider auditing their sites to make sure they are carrying out sufficient safety and risk mitigation activities.

However, if during its investigation a company uncovers environmental damage, or the threat of damage, the operator is required by law to disclose that to the authorities. Previously operators only had to disclose environmental damage if there was a specific requirement in an environmental permit.

Unfortunately there are plenty of other things for risk managers to be worried about besides the environment at the moment. For that reason the EU Directive may not prompt a flurry of environmental audits. Companies that have operations in sensitive ecosystems, areas of high biodiversity or near sites of special scientific interest, might prove an exception to this.

In the event that environmental damage occurs, companies will need to consider whether their current insurance policies cover the costs of clean-up. Insurance and risk managers should be reviewing their policy coverage to ensure that they have adequate cover. It may be that consideration should be given to purchasing a stand-alone environmental liability directive solution to provide for the extended liabilities.



The vast majority of General Liability policies currently do not cover liabilities arising from the ELD.

The new XL Insurance Environmental policy includes ELD coverage as standard, and includes

– Preventative measures
– Primary remediation
– Complementary remediation
– Compensatory remediation

Our team of Environmental specialists and consultants offers a dedicated underwriting, loss prevention and claims service, enabling the design of environmental insurance solutions to complement your own risk management practices.

The ELD is in the process of being implemented in the UK now. Call our Environmental underwriting team to make sure your company's financial exposures are covered.

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