

# SPECIAL REPORT:

# ENVIRONMENT

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# Varying shades of green

International businesses can no longer afford to ignore environmental issues and need to make sure they keep track of constantly shifting rules and regulations

**R**EGULATORS AROUND THE world are getting tougher on environmental violations. Their powers might be geared towards reducing damage to the planet, but their effect on business could be considerable.

The toll of multinational companies falling foul of increasingly stringent environmental rules is mounting as they struggle to cope with the demands of different jurisdictions. Keeping up with this rapidly changing landscape is an onerous task that catches out unwary businesses.

For every major environmental incident that makes headlines, there are hundreds of smaller ones. The fact they fail to raise a stir in the media makes them no less damaging for the companies involved. As Karl Russek, senior vice-president, environmental, for ACE Overseas General, points out, although many incidents do not make the international news, they still attract the wrath of relevant authorities and have major ramifications.

“These are not just technical issues of environmental management”, says Russek. “In an era of 24-hour news and powerful social media, an incident affects companies in terms of their reputation and their brand. That’s true [even] if they’ve not done a lot wrong.”

The main challenge for multinationals is the speed at which regulations change. For instance, Chinese authorities startled many foreign businesses in 2014, when they moved environmental issues to the top of the agenda and violations became their priority. Since 1 March, a credit rating scheme measures the efforts of many industries to protect the environment against stiff and specific standards. Under the scheme, a company’s environmental scorecard will also go straight to the bottom line – lenders will use the ratings to determine whether a client should get a new loan and, in particular, a government subsidy.

No industry is immune. Coal, transportation, steel, cement, metallurgy, chemicals, building materials, paper, brewing, pharmaceutical, fermentation, textile, leather and mining: all are subject to the new regulations. Inevitably, they will affect many multinational factories in economic zones such as the Yangtze River and Pearl River deltas, both heavily polluted areas earmarked for a rapid restoration.

Further, the Ministry of Environmental Protection, which runs the project, can include almost any business that emits toxic or hazardous materials. Previous offenders attract special and relentless attention. The government’s moves, which rate companies on a four-point system between green (trustworthy) and red (offender), are a response to mounting public ire against polluters. With pressure increasing, otherwise exempt businesses are joining the scheme to show themselves as good corporate citizens. As lawyer Ostiane Goh-Livorness of Jones Day explains, “those who do not fall within the scope of the scheme may participate of their own volition”.

## Mishmash of regulations

Evidenced by the World Bank with its green bonds and other initiatives, the momentum is gathering pace. For instance, the sale of green bonds – whose proceeds are ploughed into anti-pollution projects – increased fivefold last year to \$11.26m (€8.26m). As the bonds help pay for major infrastructure projects, companies tendering for these jobs are required to show they prioritise sustainable development. Some of the biggest multinationals are jumping aboard this environmentally friendly wagon – Ford Motor Company and Microsoft bought green bonds for the first time in late 2013.

Penalties are also rising right across the world even for small breaches. The world’s oceans and waterways are

## *‘An incident affects companies in terms of their reputation and their brand’*

Karl Russek, ACE Overseas General

under particular scrutiny. For instance, Australia, which is influential in maritime law in Asia-Pacific, has increased tenfold – to AU\$10m (€6.7m) – the maximum fines for the discharge of oily water under much stiffer, new marine pollution laws. Other countries are following suit under international maritime laws that ban the dumping of all garbage at sea and have been quick to move against offenders.

In another development, offences now give rise to criminal prosecutions, once a rare outcome. For example, after a Dutch-owned vessel leaked 200l of oil into Australia’s Newcastle Harbour in 2011, the company was fined AU\$150,000 despite no evidence of environmental harm, the offender paying for the clean-up. This was the first such incident involving the company – or the captain – in the world. As Australian firm Corrs Chambers Westgarth points out, the court took the view that “the spill was not insignificant, it was reasonably foreseeable, and it was preventable”.

In short, Australia’s courts are cracking down and targeting individuals. Although only China has introduced the death penalty for those guilty of serious pollution, other countries are taking a tougher line on offenders who acted negligently or recklessly. As many incidents show, owing to public pressure regulators are particularly tough on spills in ecologically sensitive areas.

Trouble can also be found close to home. In early 2014, Dutch food-processing giant Vion Foods’ beef-processing plant in Schleswig-Holstein, Germany, was shut down for alleged breaches of hygiene and other regulations – although six independent

audits vouched for the factory’s compliance. In March, Vion threatened legal action, demanding compensation, but the plant remained closed.

Alarming, France is about to put a principle known as “ecological prejudice” onto the statutes. According to insurers, the implications for most industries will be profound in terms of liability to different kinds of sanctions.

As the fall-out from environmental breaches shows, the legal ramifications often endure for years, incurring severe reputational and financial consequences in the process. In March, the Spanish courts fined Ferrovial and six subcontractors €21m seven years after major construction works at Barcelona’s container port for the Hutchinson group collapsed into the harbour. (The port authorities had asked for €101m in compensation.)

In this often conflicting mishmash of regulatory risks, it is unsurprising that firms increasingly seek protection across activity and geography. “Clients are looking at covering environmental risks that may be excluded elsewhere, especially within commercial general liability, construction or D&O policies,” says Julien Medina, environmental adviser for Marsh France. “They are also adjusting their coverage to follow [the path] of their business activities.”

As the price of breaches rises, for example for reputation and repair costs, insurers are boosting capacity to match. ACE group now offers a capacity of \$50m for global clients seeking cover for environmental liability, substantially up from the previous \$30m.

In this climate, protection considered adequate a year or two ago may be deficient today. **SR**

# Worth the paper it is written on

Many companies may not have an adequate level of cover in respect of environmental risks and should review their exposure to those risks and buy insurance more reflective their needs

**A**N INSURANCE POLICY IS more than a mere document, much more. Although firms increasingly have to arrange a comprehensive cover against the multiple consequences of an incident – for instance, third-party liability, physical injury, property damage, financial loss, clean-up costs, emergency expenses and business interruption – the onus is on businesses to avoid these repercussions by taking robust, audited preventive measures. As the fast-growing international case law shows, it is vital that an offending company can claim in its defence that, despite slipping up, it had adopted and executed a formal strategy to protect the environment.

As Nicolas Givelet, ACE's environmental risk engineer for continental Europe, explains, the policy should be regarded as merely the opening salvo in a company's green programme. An entire regime of risk reduction, he advises, should be built around the policy against the multiple damage that environmental accidents generally cause.

More regions are waking up to this broader concept of risk reduction.

According to ACE's recent Emerging Risks Barometer, a survey of 650 companies in Europe, the Middle East and Africa, 42% of local businesses rate environmental threats as having the potential to affect their bottom line while three quarters said their shareholders are taking them more seriously than before. Yet ACE's own research also reveals that many firms are woefully underprepared, in countries such as Turkey.

## Right level of cover

As Givelet pointed out in a speech at a reinsurance conference in Istanbul in February, many Turkish businesses have significant gaps in their environmental cover, a disturbing finding in a country with 8,000km of coastline

vulnerable to breaches. "Our client research suggests a significant level of confusion among companies on the extent of the environmental cover they currently have, if any", Givelet explains. As a first step to redress their exposure, he advises firms to conduct a thorough risk analysis of their exposure to potential environmental risks and then carefully consider whether their existing cover is adequate.

If it's not, the answer is to precisely match the cover with the perceived requirements. It's critical that businesses buy cover that reflects their needs, explains Julien Medina, environmental adviser at Marsh France. "ACE offers well-fitting coverage to clients with a good understanding of their activities," he adds.

Once the cover is in place, the next step is the all-important prevention plan. As China's sudden about-face on the dangers of pollutant industries shows, a risk-prevention regime that was considered fit for purpose a year or two ago may be quickly outmoded. Thus, consultants suggest that

businesses work backwards from the regulatory environment applying in each country rather than assume that an all-regions cover will do the job. That's because it almost certainly won't. "A multinational needs a different response according to the demands of each jurisdiction. There's no such thing as a one-size-fits-all action plan," explains one source.

Regular rehearsals of the action plan form an essential element of the preparation – and they become a crucial factor in a court room if a breach occurs. As an extra step, even the most risk-averse businesses should invite outside scrutiny of the plan by auditors and other skilled parties, for instance, practitioners in public affairs.

Some of the initiatives companies should take include: training personnel to operate well within the boundaries of the particular country's regulations; establishing a dialogue with the relevant environmental authorities rather than dealing with them as a necessary evil; developing a much-tested action plan against the

*'A multinational needs a different response according to each jurisdiction'*

occurrence of an event, however unlikely it may seem, that goes far beyond a mere clean-up. It must cover all the company's obligations towards the authorities, the affected community, non-governmental groups that may be involved, local media, public at large and any other stakeholders.

Plans should also be exposed to outside scrutiny by expert third parties.

"This must be a genuine and robust plan for containing the crisis and not something that starts with a panicky 3am phone call to the chief executive," summarises Karl Russek, senior vice-president, environmental, for ACE Overseas General. "It's surprising how few companies think about what to do until after the incident has occurred." **SR**

## France takes a controversial ecological step

**When solid cakes of fuel oil polluted France's Atlantic coastline recently, it triggered a movement that may result in an upheaval of environmental law in the country with implications for industry. With the support of green activists and government members, a principle known as "ecological prejudice" is to be enshrined in the Civil Code this year, whereby an offending enterprise will face full repair costs for environmental damage in the widest possible sense as well as maximum penalties equivalent to 10% of its pre-tax, global revenues.**

**The business would also be exposed to multiple, long-running legal actions taken by the state, environmental authorities, local governments and associations, environmental business groups and others with an interest in the "protection of nature and the environment". In effect, anybody with a stake in the particular pollution could sue because of the law's broad**

definition. "The [ecological] prejudice that we envisage is that which is done to nature, ecosystems, quality of soil etc," according to Professor Yves Jegouzo, who drafted the 10 essential principles.

The business world argue that "ecological prejudice" would add another burden to the already comprehensive legal environmental obligations. All the main private-sector lobby groups for business, insurers and big industry are uniformly hostile, arguing the government would do better to improve existing statutes, such as the law relating to environmental responsibility ("la loi sur la responsabilité environnementale"). The body representing the risk-management industry warns that the size of the proposed penalties "are likely to have a considerable impact on the survival of the business concerned". In short, a contravention of the proposed principles of ecological prejudice could prove ruinous. >>

## SPONSORED WORD

*Seventeen thousand and counting*

From Latin America and China to the European Union, environmental risk is increasingly becoming one of the major sources of concern for businesses globally.

A volatile mix of much tighter regulation, political and social pressure, emerging consumerism and intense “traditional” and social media scrutiny means that now, more than ever before, the reputational and financial damage caused by an environmental catastrophe can be immense and cost a company its very survival.

Some incidents do make the headlines – and they don’t have to be of the calibre of the BP platform explosion in the Gulf of Mexico. In January a spillage by Freedom Industries in Charleston, West Virginia left 600,000 people without drinking water and led to the company’s bankruptcy after an angry reaction from environmental authorities, local pressure groups and politicians.

This is just one example. Hundreds of incidents like this are happening every year. Most of them have serious repercussions for the firms involved. But it is important to note that the consequences can be even more serious for the middle market and smaller companies that are often the least able and least prepared to deal with an environmental catastrophe.

Meanwhile, increased stakeholder and consumer scrutiny has led to a sea change in regulation and enforcement by central governments and local authorities reacting to pressure from communities, the media and other stakeholders who demand clean water, air and soil.

Nowadays, there are 17,000 environmental regulations around the world, compared with a few hundred 30 years ago, most of them in the US. The challenge is especially complex for companies operating in more than one country or region, as regulations – but also, levels of enforcement – not only change at sometimes breath-taking speed but also vary widely. Take the example of Latin America: many countries have stiff official penalties for environmental incidents in their statute books for years now. It’s only very recently that they actually started enforcing those.

Current challenges are here to stay. Businesses – and not only in industries that “traditionally” pollute – have to manage environmental risk effectively and make sure that the insurance cover they have is as comprehensive as it can be. At ACE we want to support the evolving environmental cover needs of companies in Europe. We recently added crisis management cover to our environmental proposition. For us cleaning up your site is just one of the things a company should be covered for. In today’s world third party liability, maintaining and restoring public confidence and helping a business get back on its feet as quickly as possible after an environmental incident are of paramount importance.



Karl Russek, senior vice-president, environmental, for ACE Overseas General

## When the worst does happen

Everyone in a company should know what their specific roles are in the event of a crisis

ONE OF THE MOST REVEALING exercises a company’s crisis management team can do is to study the environmental incidents suffered by other firms around the world. Often they provide case studies of what not to do. Below is only one example of a flawed response.

When a fire broke out late last year on a landfill for non-hazardous waste in regional France, the fire-fighters promptly turned up. So far, so good. However, they sprayed water on the 40m<sup>2</sup> area, a response that is doomed to failure in a deep landfill. After three hours, the fire was raging more strongly than ever and had spread to the bottom of the site. Only at that point was the site operator allowed to dump soil on the fire – the specified technique to extinguish landfill blazes.

In the wake of one incident, painful lessons were learnt. Because of the incorrect initial procedure, it took five days to put out the fire instead of a few hours. The water had penetrated so deeply into the landfill that it required a major exercise to collect and treat the contaminated liquid.

As a result, the total cost of the claim was €200,000, instead of a mere few thousand had the proper methods been employed.

### Being prepared

The lesson, say insurers, is to have in hand a thoroughly tried-and-tested response mechanism in which all the parties know their role, including, in this instance, outside agencies such as the fire service.

Karl Russek, senior vice-president, environmental, for ACE Overseas General, has been involved in the fall-out many such incidents. He points out that far too often the response happens on the fly. “Surprisingly few companies think about what actions they should take until after the incident has occurred”, he points out. “As a result many events are terribly managed.”

According to consultants, the golden rules are straightforward: know what could happen, be ready when it does, and immediately launch communications with all stakeholders. In short, it won’t be all right on the night. **SR**

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