The background of the entire page is a photograph of an oil spill on a body of water. The oil has formed a large, swirling slick with vibrant colors of purple, blue, orange, and yellow, contrasting sharply with the dark, rippling water. The sun is reflecting off the surface, creating bright highlights and shadows.

# MANAGING ENVIRONMENTAL RISK



**Strategic**RISK

# CONTENTS

## GAPS IN COVERAGE

4-5

The onus is on businesses to be clear about their exposure to environmental risk

## ENVIRONMENTAL LEGISLATION HOTSPOTS

6-7

An outline of approaches to environmental law in the US, Europe, Middle East and China

## RISK OUTSIDE TRADITIONAL MARKETS

8-9

Even small companies in sectors not previously linked to pollution are under scrutiny

## REPUTATION DAMAGE

10-11

It's never been more important to have a policy in place to handle brand damage

## CRISIS MANAGEMENT

12-13

Environmental compliance specialist Grant Cropper has 10 tips for staying ahead in a crisis

## KEY DEFINITIONS

14

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# Managing environmental risk in today's changing business world



By Dorothee Prunier, environmental risk manager Continental Europe, ACE

The world is waking up to the fragility of its ecosystems, and the world's leaders are taking action – from US president Barack Obama's determined action on climate change to the Chinese authorities' move to repair the environmental damage caused by decades of rapid industrialisation.

There are now estimated to be 17,000 pieces of environmental legislation in place around the globe.

New laws are emerging all the time, while old laws – which may not have been enforced effectively for years – are suddenly being enacted with renewed vigour.

At the same time, a more developed appreciation of the interconnectedness of business, society, health and environmental wellbeing is bringing more and more companies into the spotlight. Industrial sectors such as retail and financial services, which may never before have been associated with 'pollution' in the traditional sense, are suddenly discovering new environmental liabilities and risks.

Meanwhile, the world waits on social media, ready to expose any industrial accident to a global audience within minutes, shooting holes in brand and reputation in the process.

With these kinds of challenges, risk managers in all sectors need to look to their risks and interrogate their insurance.

Without dedicated environmental cover there are very likely to be exposures. The

time to discover those is now. Risk managers must be confident that their international insurance programmes are structured for this multinational risk.

They must also ensure that their insurer has the footprint to act on the ground immediately and that it has the capacity to address claims at the pace demanded by the modern world.

In the end, this is not just about self-protection. In a world where brand and reputation are everything, choosing the right environmental insurance is an opportunity for a company to make a positive statement to the rest of the world about the way it does business.

Customers and shareholders are increasingly interested in seeing that the organisations in which they spend their money are doing the right thing and behaving responsibly, and many in the C-suite recognise this.

More and more companies are now seeing that managing their environmental risk is about doing more good than harm. It is an opportunity to demonstrate that risk managers are adding value to the world and delivering on the company's corporate values.

In the end, the choice is simple. At the very least, businesses must be compliant. But they can also choose to do the best they possibly can to show the world that they take the environment seriously – and proactively cover their risks.

# THE BIG PICTURE

Environmental risk involves a wider range of issues than are often expected – organisations need to be clear on what their insurance policy covers

It is a common misconception that environmental risks only relate to traditional “pollution”. However, a business could be exposed to an environmental risk if it is involved in any of the following activities:

- owns, operates or buys and sells property
- operates on third-party premises
- uses, stores, transports or produces a potentially hazardous substance that may cause contamination
- creates solid, liquid or gaseous waste
- redevelops brownfield land
- operates in a biodiverse environment, such as next to a nature reserve or protected habitat.

If any of these apply to an employer and a claim is made, the organisation may find itself dangerously exposed unless it has the right cover in place.

Companies often assume that they are covered by their general liability policy, but without specific environmental cover, they will almost certainly be left to handle a crisis – and pay for any clean-up, as well as all associated works – without the benefit of insurance.

## Risk/policy

Sudden and accidental pollution

Gradual pollution

Historical pollution

Statutory clean-up

On-site first-party clean-up

Environmental Liability Directive

Environmental damage

Loss mitigation

Incident response

Crisis management and PR costs



General liability	Property	Environmental liability
✓	LIMITED	✓
✗	✗	✓
✗	✗	✓
✗	✗	✓
✗	✗	✓
✗	✗	✓
✗	✗	✓
✗	✗	✓
✗	✗	OPTIONS AVAILABLE
✗	✗	OPTIONS AVAILABLE

# LEGISLATION HOT SPOTS

A look at different – and developing – approaches to environmental regulation across the globe

**E**nvironmental legislation can be a complex, ongoing challenge for risk managers. It is becoming an increasingly important factor to consider in almost every global market.

“It is a growing area,” says Willis environmental practice leader Richard Sheldon. “It is an area where there is a lot more awareness for various reasons, whether that is through climate change or other events. It is something that is in the news and on the radar. It is also coming into contracts more and more frequently.”

“While the US and Europe are developing their legislation, other countries traditionally seen as lax are coming up to speed rapidly,” says Cliff Warman, EMEA environment practice leader at Marsh. “Either these countries have not had comprehensive environmental laws before or they were not enforcing them particularly strictly and they are now looking for examples of best practice. This often means looking to the US and Europe. As such, much of the new environmental regulation is built around a risk assessment approach and the protection of the environment.

“Regulators appear more able and willing to take action. We have seen examples in China, for example, where the regulators have moved to close down businesses if they are seen to be damaging the environment through their operations.

“Historically, the majority of claims for environmental losses were pollution driven and were very much focused specifically on people or property being injured or damaged.”

Many losses ended up with a requirement to clean up polluted land. Warman says: “The regulations have changed and the key risk issue is causing damage to the environment, rather than simply pollution.

So, you might include those losses that lead to a fish kill or physical damage to a protected habitat. It is a much more holistic approach and we are protective of the environment in all its forms. This is very different to the polluter pays legislation we used to see.”

Risk managers tend to cope with these changes in different ways. Some look to brokers and insurers to advise on local conditions and then adapt accordingly.

“Others might take the view that best practice is the best way forward and so will do the best they can do, wherever they operate,” says Warman. “They will take the standards from the strictest countries in which they operate and apply them everywhere they work. And there are more and more of these types of firms.”

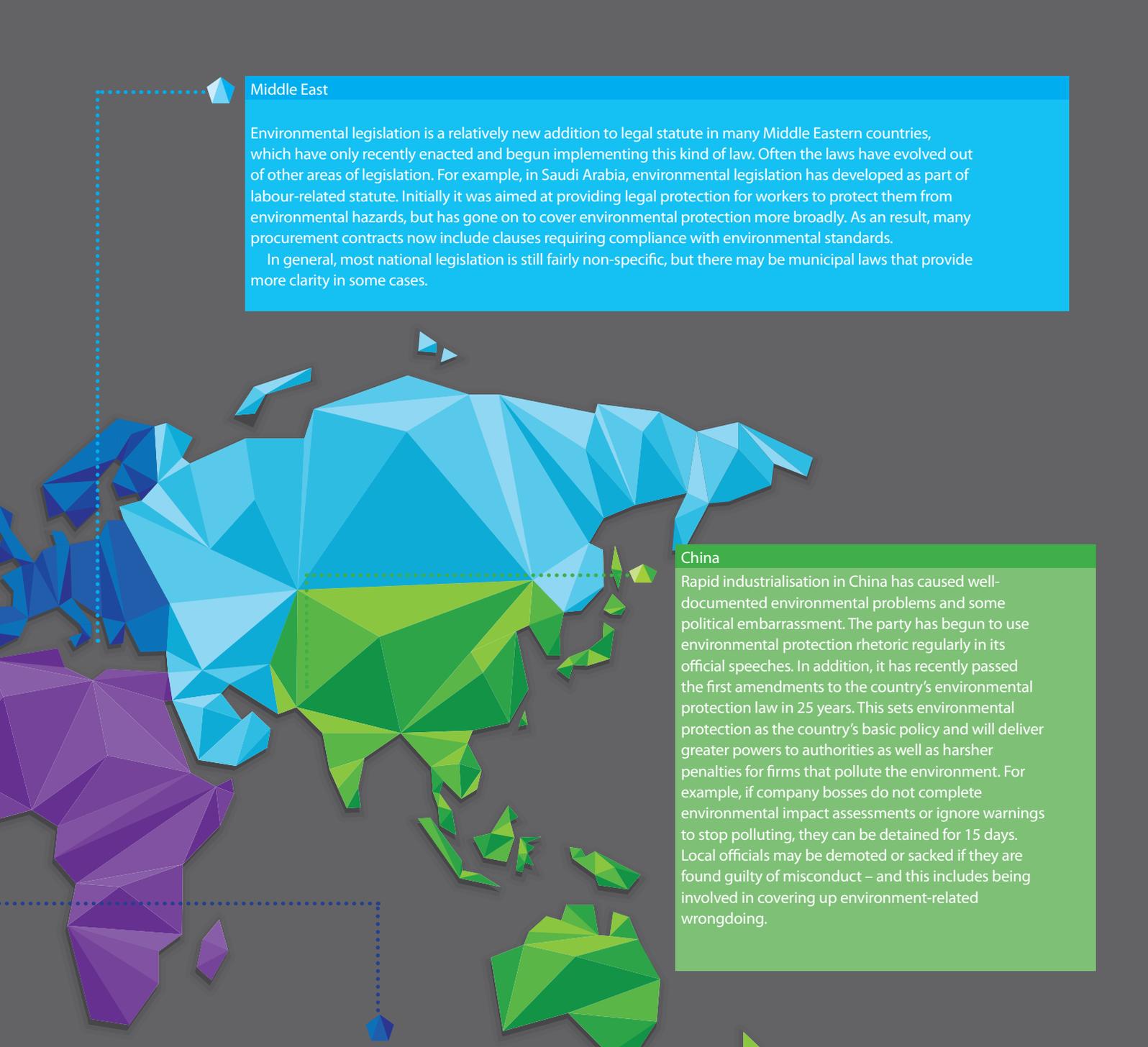
## UNITED STATES

US environmental laws have been designed to protect human health and improve the natural environment and they represent some of the best-developed standards in the world. Increasingly, they act as an inspiration for other countries looking to develop their own legislative frameworks. At its heart, the laws are intended to address pollution. But a related set of regulatory regimes focus on the management of specific natural resources, such as forests, minerals or fisheries. Other related but separate areas of law cover environmental impact assessment.

The most significant federal statutes are the Clean Air Act (air pollution), the Clean Water Act (water pollution) and the Comprehensive Environmental Compensation, and Liability Act (CERCLA – or Superfund), all of which are intended to address pollution control and remediation.

There are also federal laws strongly influenced by environmental principles that govern the management of natural resources, including the Endangered Species Act, the National Forest Management Act and the Coastal Zone Management Act.





## Middle East

Environmental legislation is a relatively new addition to legal statute in many Middle Eastern countries, which have only recently enacted and begun implementing this kind of law. Often the laws have evolved out of other areas of legislation. For example, in Saudi Arabia, environmental legislation has developed as part of labour-related statute. Initially it was aimed at providing legal protection for workers to protect them from environmental hazards, but has gone on to cover environmental protection more broadly. As a result, many procurement contracts now include clauses requiring compliance with environmental standards.

In general, most national legislation is still fairly non-specific, but there may be municipal laws that provide more clarity in some cases.

## China

Rapid industrialisation in China has caused well-documented environmental problems and some political embarrassment. The party has begun to use environmental protection rhetoric regularly in its official speeches. In addition, it has recently passed the first amendments to the country's environmental protection law in 25 years. This sets environmental protection as the country's basic policy and will deliver greater powers to authorities as well as harsher penalties for firms that pollute the environment. For example, if company bosses do not complete environmental impact assessments or ignore warnings to stop polluting, they can be detained for 15 days. Local officials may be demoted or sacked if they are found guilty of misconduct – and this includes being involved in covering up environment-related wrongdoing.

## EUROPE

Environmental protection has long been a cornerstone of European law, at national and EU level. Since the 1970s, the EU has developed a series of laws that collectively aim to compel companies to take greater responsibility for protecting the environment and minimise their impact on biodiversity.

Based on the Treaty on the Functioning of the EU, there are now laws covering waste management, air and water quality, greenhouse gases and toxic chemicals, such as the European Liability Directive, the Registration, Evaluation, Authorisation and Restriction of Chemicals (REACH), among others.

Indeed, countries that have recently joined the EU will face fresh challenges as their environmental protection practices – or lack thereof – come under heavy scrutiny. Croatia, for instance, joined the EU in 2013 and is under huge pressure to ensure it complies with EU environmental laws, with the biggest areas of improvement to be made in waste management and treatment and in the reduction of emissions and pollution.

Countries waiting in the wings to join the Union will suffer similar pressures. Turkey, for example, experienced welcomed economic growth during the 1990s owing to increased industrial production. However, this has led to higher levels of pollution and businesses will need to be aware of their environmental and legal obligations if they become members of the EU.

The country has, however, made recent improvements. A raft of new legislation was introduced with the aim of bringing Turkish legislation in line with EU standards, including:

- Amending the Turkish Environmental Law 1983 in 2006 (Official Gazette No.2872, 24 Jun 2006) with the view of harmonising its regulation with EU law;
- Enacting the Law Pertaining to Principles of Emergency Response and Compensation for Damages in Pollution of Marine Environment by Oil and Other Harmful Substances (Official Gazette No: 25752 of March 11, 2005);
- Introducing the Government Notification on General Rules for Obligatory Financial Insurance for Coastal Facilities, issued by the Treasury on 1 July 2007.

# POLLUTED WATERS RUN DEEP

No organisation – whatever their size or sector – is immune to increased environmental scrutiny

**A**CE environmental liability manager for Italy Deborah Sola is in no doubt. “Some companies still feel that environmental risk mainly affects bigger corporates or sectors that ‘traditionally’ pollute. This is certainly not true.

“With heightened media and public opinion interest and scrutiny, dealing with environmental risk should be a priority for companies of all sizes.”

Accepting this is one thing. But dealing with it is another. In Europe, there can be multiple overlapping national and pan-European regulations, while in the US, federal as well as state rules apply.

“In Italy the landscape has become very complex,” says Sola. “There is first-party and third-party liability and also now, in the case of an incident that damages the environment, companies not only have to compensate those affected, but also restore the natural habitat.

“There is even a D&O aspect to environmental risk, as executives can now be held personally accountable. And public authorities now have the right to act in advance against a company to prevent an incident from occurring.”

All this means there are additional responsibilities for companies. Every

incident now has to be reported – whether it has caused damage to a third party or not. Even with minor incidents, companies have to follow the orders of the authorities. “Failure to comply may result in mitigation actions having to be repeated,” says Sola.

She acknowledges the implications of this. “Even if a major environmental disaster has not happened, a small incident can place a serious burden on a company,” she says.

If the organisation in question is a listed company, a £200,000 claim may be relatively insignificant. But for a family firm, it could lead to bankruptcy. There are already cases where this is happening and many medium-sized firms do not have the risk management or the insurance in place to address their exposure.

“The main trend is that [the situation] is getting more and more stringent, more complex,” says Dorothee Prunier, environmental risk manager Continental Europe at ACE. “Do not underestimate it and make sure you get local advice. You need to treat each country separately and get the best advice available. You cannot rely on generalisations.”

Prunier adds: “You need to think not only about the regulations, but also about how they are being applied.”

Every incident now has to be reported – whether it has caused damage to a third party or not



## SMALL OPERATORS, BIG IMPACT

Small firms in sectors not usually associated with environmental damage can have a huge exposure to risk, as these recent examples from the Italian food industry illustrate. ACE environmental liability manager Deborah Sola describes three incidents.

- When a 60,000-litre milk tanker collapsed near a famous seaside tourist resort, the cost of the damage exceeded €350,000. The spill was not contained, entered the sewage system and ended up in the sea, causing damage to sea life and claims from hotels and tourists.
- The leak of 30 cubic metres of ammonia into a river at a dairy products processing firm caused a loss of about €250,000. Four days after the leak, the river pollution stretched 20km downstream and resulted in tonnes of dead fish and serious environmental damage.
- The malfunction of a treatment plant at a pig farm caused extensive damage to farmers. Untreated waste water from the sewage has a high nitrate concentration and, if used to irrigate the fields, can cause substantial damage. The company paid €350,000 in compensation.



## CASE STUDIES



## CHANGE OF FOCUS

As more developed understanding of the impact of humans on the natural world is leading legislators to more closely monitor sectors that previously would not have been associated with pollution. In the US and across the EU, for example, authorities are scrutinising the procedures and operations of pharmaceutical firms.

“Even small irregularities in either finished products or manufacturing processes may have implications for companies, which may lead to the disposal of entire production batches,” says Grant Cropper, environmental compliance specialist at crisis management company Red24assist.

If a firm fails to adapt to increasingly cross-functional environmental regulatory compliance, risk management and operational excellence, this will have the knock-on effect of decreasing consent, product recalls and tremendous waste, says Cropper.

## THINK ABOUT

1. Potential sources of an environmental crisis  
Is there a contamination risk on or near your business? Or within your supply chain?

2. The pathway  
How could this reach stakeholders or the wider environment, either directly or through your products?

3. The impact  
If this happened, would it result in damage, injury, or require a regulatory enforced clean-up?

If this is the case, your firm could face large fines as well as potential social and reputational damage – unless appropriate insurance is in place.

# A STEP AHEAD OF REPUTATIONAL DAMAGE

In a media-savvy world, hard won reputations are easily lost, particularly over environmental scandals. Companies must take action now to put safeguarding procedures in place

**N**o one can eliminate bad luck, and disasters can hit even the most careful firms with the best risk management policies. However, the extent to which these events go on to affect a company's reputation – and its bottom line – is down to a company's risk management procedures.

"It is essential for a business to demonstrate to the public that it is prepared to deal with the situation, take charge and protect anyone affected, whether they are customers, stakeholders or employees," says Shane Russell, malicious product tampering specialist at Red24assist.

The list of firms that have suffered from severe brand damage after an environmental crisis, either as a result of their own operations or those within their supply chain, is long. Safeguarding a brand depends on a proactive approach.

People are predisposed to assume the worst – that companies prioritise making money even at the expense of the environment. And businesses must stay one step ahead to avoid that mindset establishing itself. This is nothing new. But what has changed is that the level of awareness of environmental issues has risen enormously over the past couple of decades, with the millennial generation leading the way, as has the means by which these

concerns are communicated.

"The biggest challenge is social media and the fact that it is so easy to lose control," says Russell. "You cannot change what people post or when."

Carl Leeman, chief risk officer at Katoen Natie, says: "When it comes to reputation, one golden rule will always prevail: in these times of ultra-fast communications and electronic media, it is not a good idea to try to hide something.

"Following an incident, if a company comes out with a message first, they are putting themselves in a position where they can control the message and the information. This way, they stay one step ahead of the pack."

Now more than ever, it makes a big difference to have a crisis management plan (CMT) in place. "In the old days, a firm might get a call from a newspaper asking for a comment by a certain time of day, so they had time to prepare," says Russell. "Now

companies have to provide a more instant response – they have no time. Companies now need a media strategy."

Companies must be sure of how they will communicate – will they upload information to their website and how will they use Twitter? They have to be ready at a press of a button.

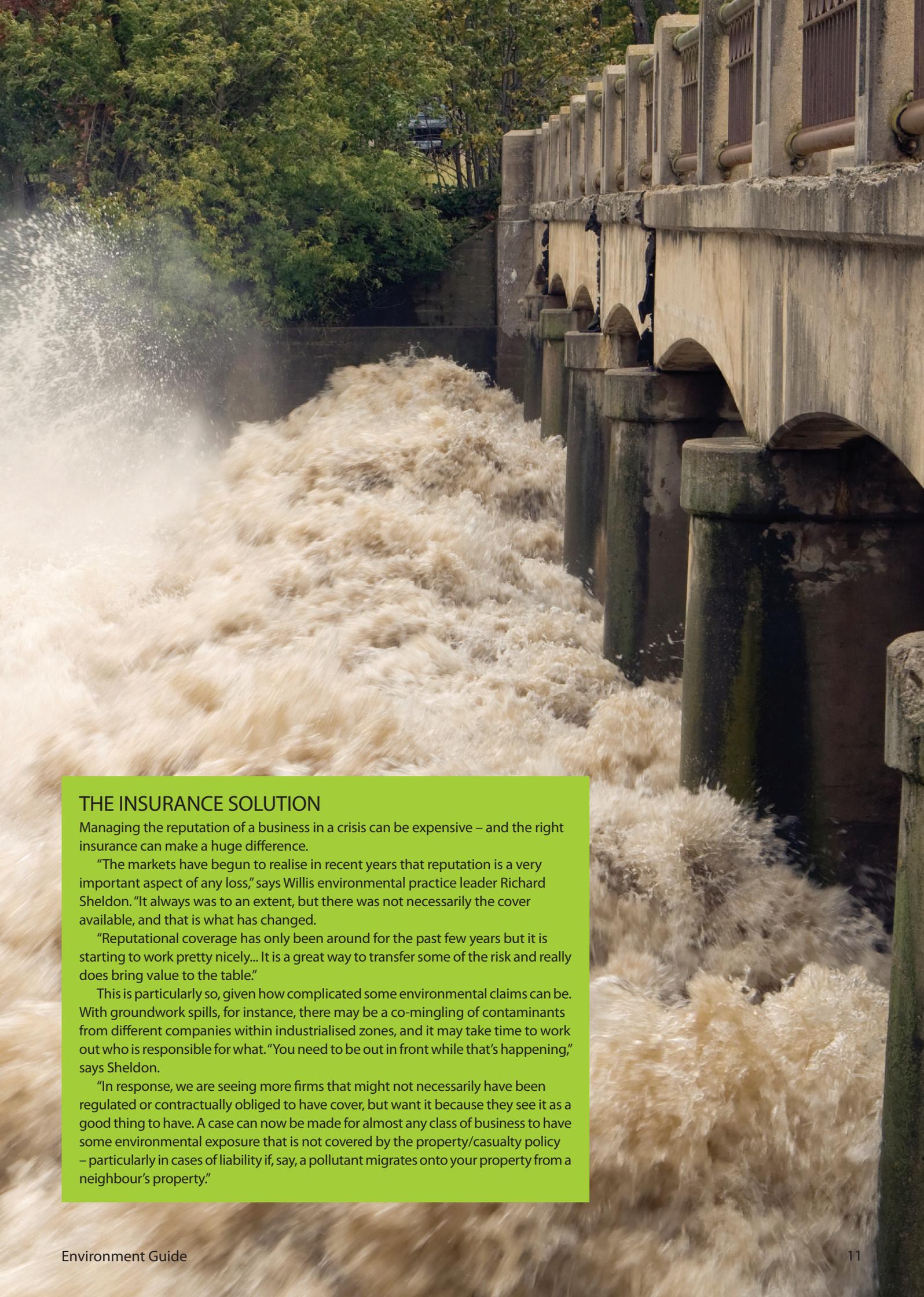
Russell adds: "Companies have to know in advance what their risks are and, although they cannot cover every eventuality, they can cover most. Think about the worst case scenario."

Supply chain management needs to be part of a firm's risk assessment. The longer it is, the more checks firms have to make. "The horsemeat scandal was a real wake-up call in this respect because it showed how complex supply chains had become and how many firms were unsure of the stages their products had gone through before they arrived on the shop floor.

"I have known firms go out of business over these kinds of claims, particularly if they are one-product firms."

Companies have to take action and be seen to take action, urges Russell. "The public is much quicker to hold companies to account over their actions. The days are long gone when [an incident] might never hit the media and you might just get away with it."

Although [companies] cannot cover every eventuality, they can cover most



## THE INSURANCE SOLUTION

Managing the reputation of a business in a crisis can be expensive – and the right insurance can make a huge difference.

“The markets have begun to realise in recent years that reputation is a very important aspect of any loss,” says Willis environmental practice leader Richard Sheldon. “It always was to an extent, but there was not necessarily the cover available, and that is what has changed.

“Reputational coverage has only been around for the past few years but it is starting to work pretty nicely... It is a great way to transfer some of the risk and really does bring value to the table.”

This is particularly so, given how complicated some environmental claims can be. With groundwork spills, for instance, there may be a co-mingling of contaminants from different companies within industrialised zones, and it may take time to work out who is responsible for what. “You need to be out in front while that’s happening,” says Sheldon.

“In response, we are seeing more firms that might not necessarily have been regulated or contractually obliged to have cover, but want it because they see it as a good thing to have. A case can now be made for almost any class of business to have some environmental exposure that is not covered by the property/casualty policy – particularly in cases of liability if, say, a pollutant migrates onto your property from a neighbour’s property.”

# TOP TIPS FOR HANDLING A CRISIS

The best advice for all firms is to be prepared, insists Red24assist environmental compliance specialist Grant Cropper

## 1 Crisis management plan

This should provide a list of contacts – legal, PR, government agencies, members of the crisis management team (CMT), along with clear guidance and checklists to stabilise the situation. This should be updated regularly.

## 2 Risk determination

Firms must have a clear appreciation of the types of risks they may be exposed to. This will assist in determining the resources required, including the individuals who would form part of the CMT, facilities and operational support.

## 3 Crisis management team

The CMT will need a range of skills, including members of senior management, environmental compliance officers, risk managers, public relations, legal experts and human resources. Each will have specific tasks, accountability and decision-making powers.

## 4 Resources

It is crucial that an organisation is prepared with suitable levels of resources. A crisis can happen any time and events will move fast. At least one person and a deputy must be available 24 hours a

day, seven days a week until the crisis situation stabilises.

## 5 Crisis communication plan

It is important when a crisis has been identified that all stakeholders and interested parties – government agencies, senior management, insurance bodies and members of the public – are given the correct information in a timely manner. Communication is crucial. An organisation will want to appear to be empathetic, congruent, positive and operating on the front foot.

## 6 Consider the evidence

When an environmental crisis occurs, it is vital to collect and collate all available evidence as this will help the organisation deal with it successfully. For consistency, an organisation should consider producing an evidence collection and retention protocol and ensuring secure storage is available.

## 7 Identify the root causes

Once a crisis situation has subsided, a company has to make sense of the factors contributing to the crisis. An investigation into the root causes of the crisis may be carried out to ensure an

organisation is best placed to defend itself from civil and criminal litigation.

## 8 Involve CMTs in post-reviews

The review team must include the CMT representatives and close liaison with legal representatives is also recommended. An organisation has to be fully compliant with any formal legal requirements that may exist.

## 9 Produce a post-crisis report

This will represent closure to those outside an organisation and demonstrate the firm's transparency. Providing an action plan and allocating areas of responsibility for implementation represents an excellent way for an organisation to move on from a crisis.

## 10 Areas for Improvement

Acting in a positive way to move forward is essential if an organisation is to survive the effects of a crisis. For example, training or retraining staff is a common recommendation. It is also important to re-issue policies where appropriate. Also ask whether the business has allocated sufficient resources to the situation. If these are lacking, an organisation may be vulnerable to a crisis in the future.

# KEY DEFINITIONS

## POLLUTION CONDITION

The discharge, dispersal, release, escape, migration or seepage of any solid, liquid, gaseous or thermal irritant, pollutant or contaminant, including smoke, soot, vapours, fumes, acids, alkalis, chemicals, fungi, hazardous substances, hazardous materials and waste materials into or on land structures, the atmosphere, surface water or groundwater

## PREMISES POLLUTION LIABILITY (PPL)

Provides coverage for Insured locations, including foreign operations and subsidiaries. PPL programmes can be designed to cover historic contamination of property assets and the legacy risk presented when those assets are acquired through investment or M&A or divested. Operational environmental risks created by the ongoing business are also insured, including biodiversity or natural resource damage

## CONTRACTORS POLLUTION LIABILITY

Provides coverage for liability arising out of covered operations. Covered operations can include a vast range of activities, from facilities management to heavy civil construction

## REMEDIATION COSTS

Reasonable expenses incurred by the insured with the written consent of the company in the investigation, characterisation, quantification, monitoring, abatement removal, disposal, treatment, neutralisation or immobilisation of pollution conditions covered by the policy to the extent required by environmental law and as a result of a regulatory action

## REPLACEMENT COSTS

Costs or expenses necessarily incurred in the repair or replacement of buildings or structures due to damage sustained by such buildings or structures in the course of responding to a pollution condition or biodiversity damage covered by the policy, but excluding any costs or expenses incurred in respect of any improvements or betterments to such buildings or structures

## BIODIVERSITY DAMAGE

Covers any expenses incurred by a company in treating a protected space or habitat that has been affected by that company's operations. Under the Environmental Liability Directive polluter pays principle, companies are responsible for restoring any protected habitat to its original condition if it has been affected by activities that company has coordinated. This could include treating soil through to spending money to restore a habitat's humidity or range of wildlife. This area of coverage has grown recently, as a result of the greater responsibility placed on companies by the Directive

## FIRST-PARTY LIABILITY

An important strand of coverage because environmental incidents will typically affect an insured's own property first, and many forms of pollution can lead to a sizeable decrease in the value of that company's property, which may require remedial work

## THIRD-PARTY LEGAL LIABILITY

Covers a company against the costs relating to an injury or other environmentally-based damage caused to a third party. For example, it covers a company if its operations led to toxic smog release that affected the health of a neighbourhood

## SOURCE

The 'cause' of contamination, which may relate to an activity undertaken as part of a client's business

## RECEPTOR

If a 'source' is to result in damage or injury or require regulatory enforced clean-up, it must reach – or have the potential to reach – and have an impact on a receptor



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