Creating environmental security

ENVIRONMENTAL INSURANCE

Environmental sustainability is created through Environmental Insurance as it compliments a sustainable and built environment. Without environmental insurance the costs of rectifying environmental events weigh too heavily on society's ability to afford the recompense.

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Environmental Insurance

Anthony Saunders is a general insurance broker and specialises in the identification of environmental liabilities. In this paper, he discusses how environmental sustainability is created through Environmental Insurance and that it encourages energy abatement. Without environmental insurance the costs of rectifying environmental events weigh too heavily on society's ability to afford the recompense.

When Deepwater Horizon was destroyed and sank a couple of kilometres onto the seabed no one was prepared for the disastrous consequences resulting in tens of millions of barrels of oil spilling into the Gulf of Mexico over 5 months.

The importance of identifying potential Environmental liabilities is critical in the *process* of risk mitigation because an entity should assess if they are asset rich enough to financially provide for adverse environmental impact or if they should arrange to offset the potential liability that they may have with insurance. Why? The *process* highlights the investment necessary to exact precautionary measures to protect the environment.

The types of *industry categories* that have environmental liabilities:

Automotive	Exploration	Recycling	Research Rural Industries
Aviation	Fertiliser companies	Research Cotton	Research Sugar
Buildings and property	Laboratory	Research Dairy	Research Universities
Chemical companies	Landfills	Research Fisheries	Road and rail
Commercial	Mining/Mineral processing	Research Grains	Shipping
Defence	Ministerial Councils	Research Grape and Wine	State Governments
Developers	Petrochemical	Research Horticulture	Telecommunications

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Energy	Pharmaceutical	Research Land and Water	Waste management
Extractive Industries	Power	Research Meat and Livestock	Water authorities

If the entity has never considered environmental risk mitigation it's likely that their insurance excludes environmental liability.

How do we know this? Environmental Liabilities are commonly excluded by all insurers. The exclusion is known as the "Pollution Exclusion".

If you seek to get the cover, you need to speak to an insurance broker as they are able to search for the specialists who can help them arrange the cover.

Once in place, environmental liability insurance helps to create peace of mind for all concerned. How does this work you may ask?

Let us use the *industry category* "Exploration" as an example. Six months prior to the Deepwater Horizon event a similar uncontrolled oil release occurred in the East Timor Sea spreading oil over 450 square kilometres. Risks were taken by using an inadequate "blow out" preventer. Had environmental liability insurance been in place, it is argued that the incident would never have occurred, due to the insurance requirements mandating that robust risk protection measures needed to be deployed *prior* to exploration. It has been documented that the cost of building a blowout preventer that could adequately handle the pressures at depths of 1.5 to 2 kilometres on the ocean floor and a further kilometre or more into the sub strata would make the cost of exploration unaffordable.

It's not the cost of environmental liability insurance that is the stumbling block it's the precautionary measures needed to be deployed that can make exploration unaffordable.

It is obvious that oil *exploration* is an inherently risky business but we need oil to sustain world infrastructure? Mandating environmental insurance could make energy exploration (at sea) unaffordable due to the high cost of robust risk mitigation. It's not the cost of environmental liability insurance that is the stumbling block it's the precautionary measures needed to be deployed that can make each and every *industry category* safer.

Hindsight is wonderful if we can learn from it, yet exemptions continue to apply to certain industry categories *at law* making prevention as a fact difficult to enforce. Effectively without environmental insurance the industry categories can continue to operate with little or no regulation.

Remediation: A term used to describe environmental clean-up! In insurance terminology this would be defined as "Reinstatement subject to commercial consideration to limit the amount an entity would invest within their legal requirements". [NB: *Re*-mediation also suggests that the influence of pollution will slowly attenuate compromising the extent to which reinstatement may be exercised.]

Whereas "reinstatement" means to return the environment back to the way it was prior to the incident happening. However, due to the difficulty in cleaning up toxic spills and waste, the process is rather slow, and sometimes, in some communities the clean-up can take scores of years e.g. it has been revealed that Gulf of Mexico could take 3 lifetimes to recover. It is unlikely therefore that resilience levels relating to the speed of ecosystem recovery had not been determined in the case of a worst case scenario in the gulf.

Depending also on the Environmental Laws that prevail on the day (or the country in which the contamination has taken place), the level (or standard) of remediation that takes place will also vary substantially according to the resilience of ecosystems affected. For example, one should *Google* the Ok Tedi Mine.

As a result, the term remediation is used to describe a process which can include:

- Dig and dump (remove the contaminants to a place of containment)

- Natural attenuation or dispersion (leave it for long enough and the contamination will slowly “dilute”)

- On site remediation (action a plan to reduce the contamination on site)

But, do we want to keep on remediating or do we wish to stop the contamination in the first place? To answer this question we have to look at causes of contamination.

What causes contamination to occur? Most of the time, the contamination is caused unwittingly but it’s timely to become prepared. Why do you think that the state governments have imposed fines and penalties for throwing rubbish out of cars? Have we forgotten that we have ashtrays and garbage bins for a reason? Why are governments restricting development activities to contaminated sites?

Here are just a few more areas to consider where we can reduce waste and contamination risk potential. Ponder on these:

- **Automotive:** The underground storage tanks (UST) of service stations develop leaks. On average there are 9,000 UST’s in each state, and over time they leak systemically in various degrees. Many are the centre of major litigation disputes and the cause of groundwater contamination. *NB: Service station owners are responsible for reporting leaks due to the high level of contamination risk to aquifers*.

- **Commercial:** Dry Cleaners use cleaning liquids that can be stored in UST’s or above ground. The liquid used to clean garments is very effective at stain removal; it is also the centre of *international* concern due to its invasive properties and ability to migrate (pass through) dense material including concrete. It disperses easily in water and is a known deadly carcinogen. Some of the costliest litigation disputes are a result of dry cleaning liquid release. In the **Premier** Building **v Spotless** Group Ltd & Ors (Ruling No 10) [2007] VSC 68) the Financial Review reported that litigations costs exceeded $70 Million.

- **Waste Management:** Sites operated as waste outlets including tyres, spent dry cleaning fluids, hair salon chemicals, oils, and other toxic waste must be able to contain the contaminants in case of fire. Without approved site protection (bund walls) the release of toxic waste mixed with fire brigade water or foam (Fire Water) creates contamination risk. These facilities must be licenced to carry certain amounts within their licencing boundaries. Refer: Hamcor Pty Ltd and Anor v The State of Queensland and Ors [2013] QSC 9

- **Commercial:** Hair salons use chemicals to treat hair (peroxides etc.) are toxic and in some instances the runoff from rinsing has to be contained. Chemicals in dyes and rinses are required to be stored.

- **Extractive Industries:** Include plastic drink bottle and bag manufacturing. Now, there is a city in South Australia that has banned altogether the sale of plastic bottled water. We are surrounded by so much plastic there is an ocean vortex north of Hawaii the size of Tasmania. It's called the Great Plastic Vortex. The general global trend is to assess impact on oceans and contend with macro and micro levels where plastic is being absorbed into our food chain.

- **Mining/Mineral Processing:** The State and Federal Governments are increasingly interested in encouraging mining companies to provide for closure. Active and ongoing environmental management plans must be created, and funds must be provided for closure (rehabilitation) to provide for a sustainable environment.

Corporate Responsibilities:

A company's environmental compliance is regulated through international, Federal, State and local Government Acts, Regulations, Policies and statutes. Pollution Law in Australia (Zada Lipman, Gerry Bates, Lexis Nexis Butterworths, 2002) documents thousands of pollution law cases (e.g. events, accidents, errors) giving rise to the evolvement of specialist environmental law courts. The scope of these laws also encompasses the areas of carbon emissions management and reporting requirements; contaminated land management and remediation; energy production, use and abatement; waste, hazardous waste, waste management and minimisation; water security; air quality and purification; noise management and its avoidance. The list goes "on and on" and affects all *industry categories*.

Are you in doubt as to whether your insurance policy will respond to the dynamics of pollution law? What does the "Pollution Exclusion" mean if you find it in your insurance policy? What remedies do you have if a claim is brought against you and it is pollution related?

Failure to understand and comply with environmental obligations may result in liabilities including significant penalties for any entity that avoids (or is ignorant of...) its responsibilities. Ignorance is no defence.

If Section 26 of the Corporations Act takes away the "no knowledge" rule as defence and if the International Accounting Standards Board is (already) appealing to entities to be accountable for their environmental liabilities can the insurance sector claim to have a responsibility to insure a sustainable environment? It would make sense that an entity insured for their environmental risks would be considered as responsible?

What is Environmental Insurance?

It is "fail safe" insurance policy that provides the funds to reinstate the contaminated environment to a level that is in keeping with the expectations of the laws that prevail on the day and "as a fact". In the absence of such laws, common sense or "fact" ought to apply or International Environmental Standards should be adhered.

Important: Remediation should result in a satisfactory outcome where parties involved should consider the future use by next generations.

Commercial definition: Environmental insurance covers the costs related to any unexpected pollution that has harmed the environment, built or otherwise.

Technical Definition: Environmental insurance covers the financial cost incurred by an entity as a result of a fortuitous pollution risk necessitating ***precautionary action***.

Historically:

Since the recognition of *climate change* and the advent of legislation towards greenhouse gas emission reduction and carbon trading the world has woken to the fact that environmental security and the protection of our environment is unavoidable.

Can we reduce our pollution and at the same time increase production efficiency and measure an increase in profit?

"Industry appears to conjure barriers of entry into a new climate change economy suggesting reluctance to doing something new. Our economic model is challenged by environmental responsibility and the limited nous to collectively address a direction towards sustainability" (Desiree Lucchese).

Insurance company Pollution Exclusions are therefore a reaction to limited education on what truly constitutes an insurable pollution loss versus the deliberate act of polluting. The robust examples of *industry categories* identify areas where the environment is knowingly and deliberately being contaminated at our expense *en masse* and subsets of the *industry categories* include most motorised travel, dry cleaning, hairdressing, lighting, air conditioning, fuel storage of any toxic substance, any aerosol (most pressurised with natural gas), plastic bags, plastic bottles or containers, tooth brushes, light bulbs, alcohol, mixers… the list goes on.

So, it's quite a complex affair to consider how an insurance company can provide cover for environmental liability when much of the environmental contamination occurring can be of a deliberate nature?

However, just a little education helps to understand the benefit to our environmental security of making Environmental Insurance inclusive in all policies and responding to what we were not in control of.

Environmental Security, how do we create it? Try this quick quiz! Imagine that you are the owner of a service station. At the end of the day, you realise that you have less fuel in the UST than what has been sold. Do you:

a) Increase the price of the fuel to cover the loss? or

b) Contact a real estate agent to sell the site? Or

c) Consider investigating a possible spillage loss?

Answer: Service station operators have a duty to report a possible contamination to the EPA but may avoid reporting if it means that they could incur a fine or penalty or a notice to clean up.

Fortunately, the cost of UST rectification is not as expensive as the potential claims and fines and penalties that could arise if the owner/operator of the service station does not follow some simple rules:

1. Record the date of the leak and the amount that has gone missing the day it first happens.

2. Report the matter to the EPA (Environmental Protection Authority) and confirm action is being taken or ask for guidance, or

3. Contact an environmental consultant to find out just how bad the leak is and whether it has migrated to neighbouring properties.

If the service station owner had no insurance, he or she may be scared to report. Environmental Insurance can remove the fear of reporting and cater for unexpected pollution.

What encompasses the definition of pollution?

1. Anything that may adversely affect the sustainability of an environment.

2. An act by an entity that negatively affects the sustainability of any environment or species.

3. Carbon pollution emissions released into the atmosphere.

What is Pollution risk?

Commercial definitions include:

1. The accidental release of a pollutant into a built or natural environment.

2. The failure to limit the controlled release of a pollutant into the environment as a fact.

3. The deliberate release of a pollutant at risk of a fine or penalty

Technical definitions include:

1. The fortuitous release of a pollutant unto the environment, built or otherwise.

2. The non-fortuitous (deliberate) release of a pollutant unto the environment, built or otherwise

3. Intentional or unintentional release

Is there a strategy behind the introduction of Environmental Insurance?

Environmental Insurance has been created because most insurers exclude environmental liability from their policies. The exclusion is commonly phrased as “The Pollution Exclusion”.

The Pollution exclusion is commonly found in the section of many policies under the heading “exclusions” or “what this policy does not cover”.

In order to arrange for this exclusion to be reversed, insurers first need to know that the entity seeking cover understands what they need to do to demonstrate how their pollution liabilities or risks have been (or can be) abated.

Environmental Insurance has been created so that we can provide the means to create a sustainable environment (built or otherwise).

Does Environmental Insurance encourage progress in the new climate change economy?

Earlier, we discussed that changes in economic models need to incorporate the impact on climate change. The *industry categories* listed reflect economic activities but not necessarily progress as true progress can't be measured by not accounting for externalities. Integrated Reporting identifies true progress where the outcome is to achieve pollution or carbon emission reduction.

There is a wide variance in laws around the globe pertaining to the damage versus reinstatement and restoration of the environment as a result of *industry category* practices. What is legal in one jurisdiction may not be in another. What is an acceptable level of environmental degradation in one country may not be permitted elsewhere. Further, what we know to be safe today may well prove detrimental tomorrow.

Not all environmental damage is deliberate and wilful, nor all conduct deceitful. Environmental degradation may be well unavoidable under certain accepted and lawful *industry categories* of today. *Industry categories* of such include open-cut coal or gold mining with their enormous scars on the earth and toxic waste management, or businesses such as petrol stations with their underground fuel storage tanks, risk negative impacts on their immediate and global surroundings. It's important to list producers of oil, gas and ethanol, coal-fired power stations, sugar mills (cleaning processes) and there are many more.

Deforestation, contamination and saline intrusion are common by-products of progress. Oceans too, have become sinks for waste from shipping, chemical and mining industries, urban development, farming and increasing global warming induced by acidification (CO_2 absorbed and endangering food chains). Even desalination plants, whilst considered vital in some countries, create increased salination due to ocean outfall affecting the ocean's ability to act as a carbon sink (look up "Absolute Salinity") plus the huge energy load unless powered by renewable energy.

Whilst certain activities may be legally acceptable – at the moment – Environmental (activists) lobbyists suggest that economic modelling may one day come to rationalise that the profits generated as a result of certain environmentally unsound practices, to be in direct proportion to the expense related to the necessary environmental restoration. [Part of the carbon offset debate].

The Precautionary Principle:

In 1987 the greatest invention known to mankind was invented that would improve the pollution emissions of vehicles worldwide and it was called the catalytic converter. It is referred to as an "end of pipe" solution, not actually addressing the true problem being the engine itself which radiates heat, emits carbon pollution and leaks oil. Had it not been invented would we have sought to address a "bottom of pipe" solution sooner? Do we have responsibility to dispense with fossil fuels?

Many argue pollution ought to be avoided as a 'Fact' rather than by measures 'At Law', meaning it must be limited to a common standard, not just local jurisdiction. In reality, even if a resource project is sustainable as a matter of law, it will arguably not be sustainable as a matter of fact because our current consumption levels of energy and water already exceed the sustainable yield thresholds for these resources.

If a project poses significant environmental *damage* as a matter of fact but not of law should it invoke a precautionary obligation on environmental consultants to alert entities that knowingly or deliberately contributing to such *damage* may result in litigation? If the foundation of insurance is to mitigate loss as a precaution rather than to wait for scientific evidence to prove that action ought to be taken are we not in breach of our obligations at law as a fact? It would be advisable to get legal advice on how to reduce future liabilities associated with any project that may create environmental damage. The precautionary principle of insurance applied to mitigation suggests that we have a responsibility to support pollution reduction as a fact.

Responsibility of Directors and Officers:

Many insurance companies have reacted to uncertainty over future liability regimes by limiting from their insurance policies any claim resulting from breaches of pollution, environmental or climate change laws.

Specifically, Directors and Officers (D&O) Liability policies exclude cover for the liability arising from the entity's Pollution law liabilities through the course of business, if cover ought to have been arranged under another policy of insurance. The exclusions are commonly referred to as "Absolute/Pollution Law Exclusions".

Directors and officers may be unaware that they are not commonly covered for the mistakes that their entity could contribute to or make meaning that there may be no cover to remediate the environment. Therefore the entity itself may not be sustainable?

That's where environmental insurance comes in. Environmental insurance is designed to provide for the reinstatement of the environment where it may be required to respond to inherent yet unforseen liabilities that may befall stakeholders or their principal entities.

Without it, such businesses may be considered as conducting themselves with an element of reckless regard to the environment or "self-insuring" which may result in their environmental liabilities exceeding the full extent of the liquidated asset value of the business. If "Self-insurance" is defined as acting in the same capacity as if you were the insurer then a business must be accountable and account for its externalities and they can do this through Integrated Reporting (refer A4S, The Prince's Accounting for Sustainability Project).

Environmental Insurance availability:

Insurance brokers might need to go offshore to Lloyd's to find an environmental insurance specialist to arrange covers as there is precious little resource locally available in Australia but availability is improving with new insurers claiming to be providing the cover.

But as the risks associated with being in any business today carry with them a growing carbon footprint, environmental insurance covering any environmental/pollution/climate change law is a key component in the business' sustainability.

The complex nature of covering pollution risks is that we are all polluters so it is by nature very important to understand what will actually trigger a claim under the policy and then making certain that the insured understands their obligations in order to obtain insurer protection.

Our best investment is in insurance companies prepared to cover Environmental Insurance to create a sustainable economic environment.

If you have an interest in getting access to Environmental Insurance, it is suggested that you contact your insurance broker today.