



Environmental regulators flex their muscles



There are numerous misconceptions surrounding environmental liability. This includes an assumption that pollution is just a concern for heavy industry and that most pollution losses will be covered under general liability policies. There is also an understandable belief that the polluter, and only the polluter, will be held accountable to rectify damage they have caused to the environment, with a growing emphasis on full ecosystem remediation.

AIG's latest claims whitepaper puts many of these myths to bed. The loss numbers illustrate that a broad range of environmental incidents triggered losses under AIG Europe Environmental Impairment Liability (EIL) insurance products in 2016. Claims notifications emanated from a wide range of industry sectors, and in some instances where the polluter could not be traced, it was the property owner who bore the brunt of the clean-up costs. Many events, including gradual and off-site environmental damage, would not have fallen within the scope of conventional liability products.

Claims data captured in 2016 suggests that buyers are becoming better educated about the scope of EIL coverage and their duties under current regulation. It is clear that many of the principles enshrined in the EU Environmental Liability Directive (ELD) are shaping EIL insurance claims experience. And yet none of AIG's EIL notified events in 2016 were brought under the ELD, suggesting a continuing preference for more established environmental legislation in many European countries.

A handful of incidents in Italy and Spain, which involved biodiversity damage, and could have reasonably come under the scope of the ELD, were not pursued in this manner by the local regulators. AIG's findings support those of the European Commission in its 2016 report which considers around 1,245 confirmed incidents of environmental damage across the EU between April 2007 and 2013, which triggered the application of national rules transposing the ELD.

### At a glance

- EIL claims spread across a wide range of industry sectors
- Both frequency and severity of losses on the rise
- Regulators pursuing property owners where polluters cannot be found

## Inconsistent application of the ELD

Looking ahead, Eastern European countries may prove to be one exception to this trend, as the region did not have existing environmental protection regulations before the ELD was transposed by EU member states in 2007. An EU report published in April 2016, noted that 86% of the ELD damage cases reported out of the 1,245 were in Poland and Hungary.

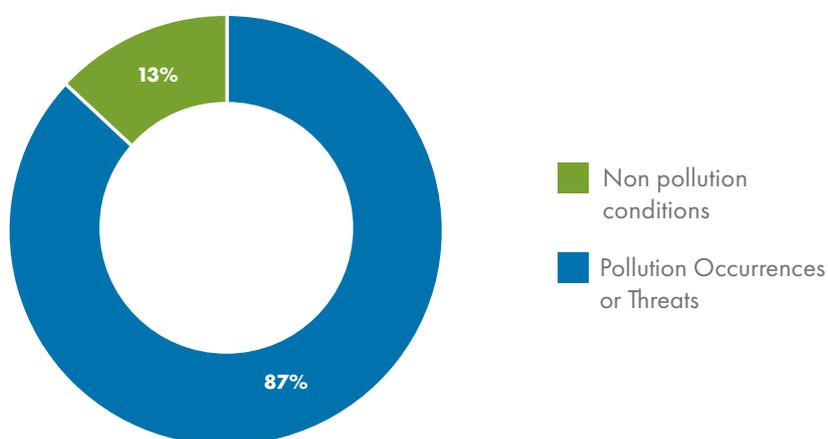
“We still observe an inconsistent application of the directive and compensation methodologies,” observes Julien Combeau, Client Risk Solutions (CRS) Industry Services Lead for Europe, at AIG. “The ELD is still quite a new piece of regulation and in some instances competes with legal frameworks that have been there for 40 years in some Western European countries.”

“As local environmental enforcement agents get more familiar with the use of the tools provided to them by the ELD, you would expect to see complementary or compensatory remediation used more and more in order to satisfy the clean-up and restoration of the environment,” he continues. “This is going to increase the cost, complexity and the time it takes to settle EIL claims.”

While none of AIG’s claims in 2016 were brought under the ELD, the Directive’s broad scope and strict remediation requirements are reflected in the loss statistics. As illustrated in Figure 1, the majority of notified events during 2016 were pollution occurrences or threats (87%), rather than non-pollution environmental damage. However, the fact that 13% were non-pollution is a significant development in itself, thinks Combeau.

Non-pollution events were characterised by direct damage to biodiversity, reduction in surface water flow and noise emissions. The non-pollution notified events under AIG’s policies also included mitigation expenditures, consequential business interruption and legal defence. “This is something that didn’t exist before the ELD,” explains Combeau. “The level of liability associated with pure environmental damage didn’t exist seven years ago, but it is now starting to impact our claims experience and the losses we observe.”

Figure 1: Proportion of Pollution versus Non-Pollution Conditions 2016 – Notified Events



### Case Study: Belgium

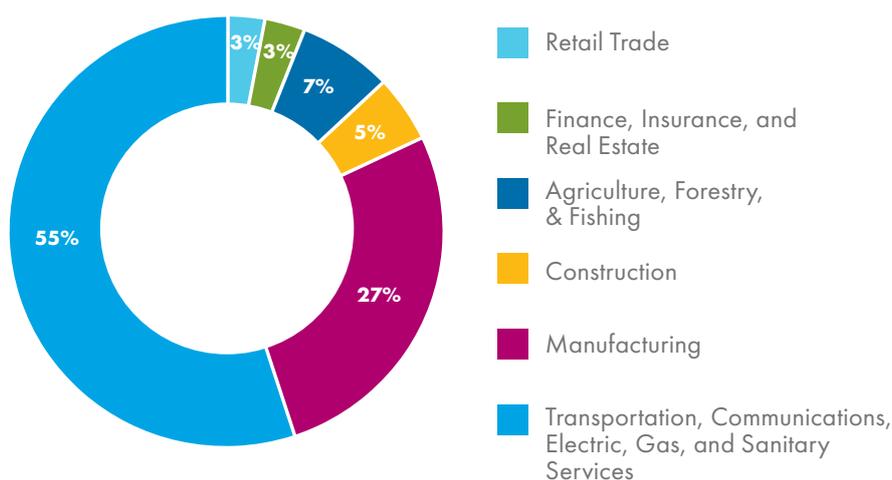
The insured, a manufacturer of digital imaging products and systems for the print and healthcare sector, was mandated by the regulator to remediate chlorinated volatile organic compound (VOC) contamination of on-site subsurface soil in addition to an off-site contaminated groundwater plume. The contamination was caused by gradual releases during the course of the insured’s operation of its facility.

## Pollution costs not just a problem for heavy industry

There were over 100 notified events in 2016, spanning approximately 30 Industrial Major Groups incorporating a wide range of sector activities from fuel management, wastewater management, waste management, transport and conveyance, finished product management, and asset management & maintenance. Parties bearing responsibility for environmental damage and pollution incidents in 2016 (and remediation costs) ranged from very large corporates through to small and medium sized enterprises (SMEs).

Notified events also emanated from a wide range of industry sectors, including a number which experienced few EIL losses before the introduction of the ELD. Figure 2 shows the breakdown of notified EIL events by industry division, with the greatest number of claims (55%) emanating from Transportation, Communications, Electric, Gas and Sanitary Services. Within this broad sector, Sanitary Services accounted for the majority of notified events, followed by local and suburban transit, water supply services and waste management services.

Figure 2: Percentage of Notified Events (2016) by Industry Divisions



Dawn Slevin, Environmental Manager Europe, Client Risk Solutions, at AIG contributed to the compilation of last year’s notified event statistics. She notes that a range of industry sectors are being impacted by environmental incidents. “These impacts go right across AIG’s client base, in both high risk and low risk industries,” she says.

## Case Study: Spain

The insured, a company engaged in hydrocarbon and fuel supply, was held responsible by the authorities for remediation, when a spill of 36,400 litres of kerosene from the insured’s tanker occurred during a theft attempt, impacting a nearby river and off-site property. Total remediation losses included clean-up costs and compensation for third-party property damage.



Analysis of the insured’s environmental risk management activities associated with notified events reveals the areas that are proving most problematic. Wastewater management and fuel/petroleum management are the most common source of a notified event, followed by waste management (on-site), and transport and conveyance. As a result, a significant number of notified events in 2016 emanated from public utility companies (including waste, wastewater, water supply and energy supply services).

Wastewater events associated with municipal treatment plants were regularly associated with obstruction of the collection systems with debris including wood, sand, and rubble, which caused backflow, overflow and migration to surface waters. Other factors leading to pollution incidents included direct physical damage to a network, failure of pumps (regularly associated with blockage) and overflow of raw sewage at the plant.

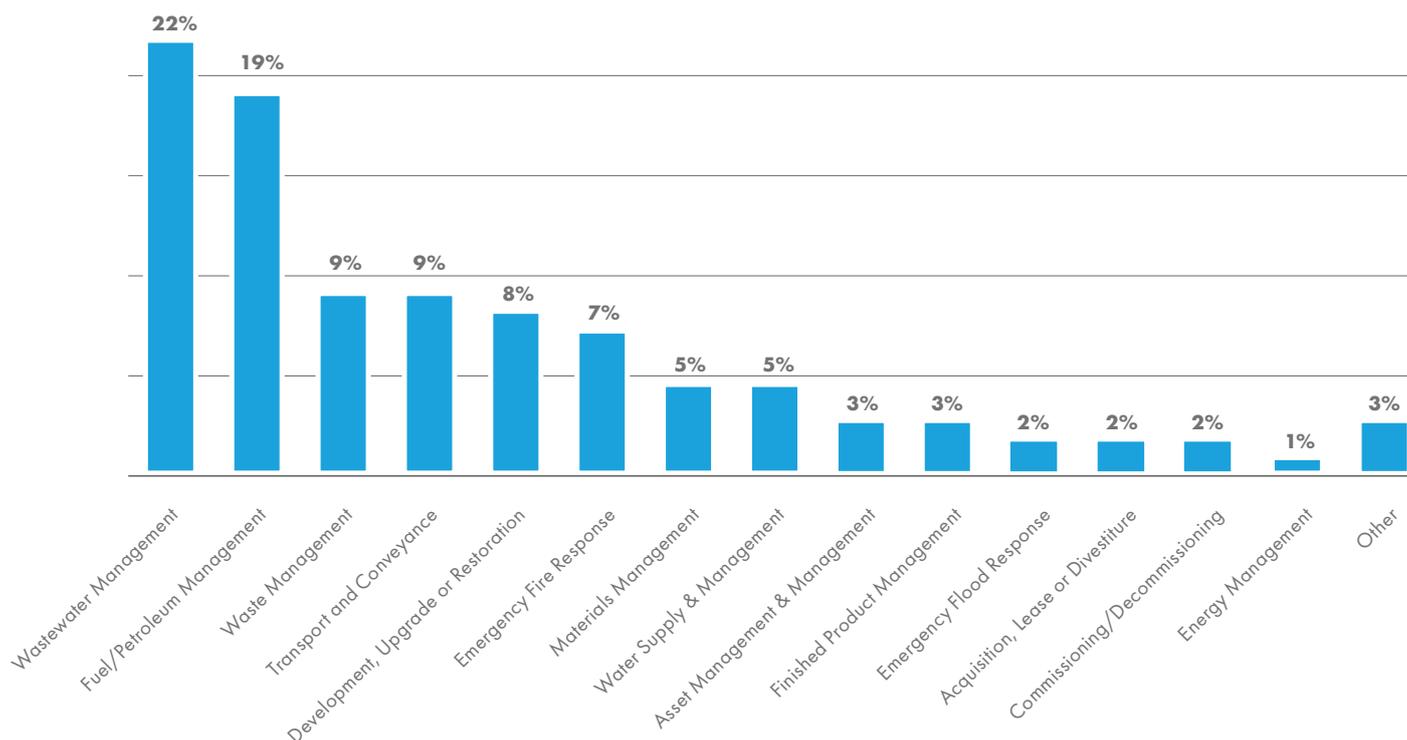
Thames Water’s record £20.3m fine, in March 2017, from the UK’s Environment Agency for repeated discharges of raw sewage from their networks is indicative of an altogether tougher regulatory stance. It also illustrates a change in sentencing, after previously lower penalties were deemed to have failed as an effective deterrent.

This tougher regulatory stance may be anticipated to continue across European member states following the European Commission’s Environmental Implementation Review (EIR) published in February this year. This review identified that most EU member states struggle to reach full implementation of urban wastewater treatment legislation. Good practice is however moving towards a risk-based regulatory approach in which the best mix of monitoring, promotion and enforcement is directed at the most serious compliance problems.

**Case Study: France**

The insured’s subcontractor, working on the construction of a highway, inadvertently drilled through high voltage cables releasing approximately 1,000 litres of insulation oil. The regulators required clean-up of the impacted soil at a significant cost to the insured.

Figure 3. Insured’s Environmental Risk Management Activities associated with Notified Events (% of Total Ranked)



## Contaminants of concern

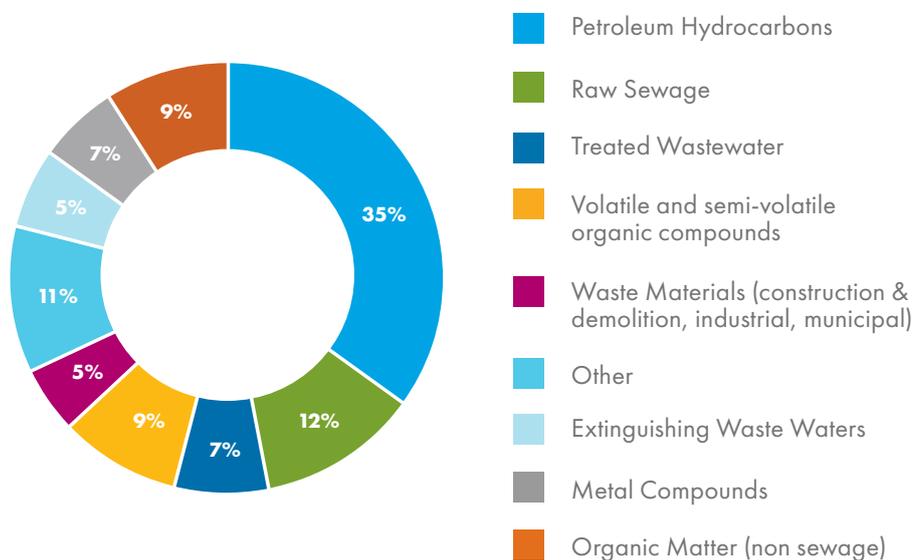
Petroleum hydrocarbons were the contaminants of most concern for 35% of AIG EMEA’s notified environmental events in 2016. “Fuel management is a big concern in almost any organisation – it is used for everything from fuel for heating and process operations and in the construction industry for machinery/plant operations,” states Slevin. “It is a common contaminant and can be overlooked.”

A number of contaminants, including chlorinated hydrocarbons, are persistent in the environment. By definition, such compounds are resistant to being broken down through chemical and biological processes.

A particular characteristic of chlorinated hydrocarbons (sources of which include agricultural pesticides and spills from chemical facilities) is how long they can persist in the environment. Many of these compounds, which are very toxic to both vertebrates and invertebrates, tend to build up in the food chain. Contaminants that remain in the environment for a long time can potentially be an ongoing source of impact and, as a result, clean-up tends to be more complex and costly.

A wide range of contaminants triggered notified events in 2016. The containment of water and chemical run-off following fires was the cause of a number of pollution incidents, both those that occurred on-site and during transportation. Overall, emergency fire response was responsible for 7% of notified events, and many of these events resulted in extinguishing waste waters being the primary contaminant of concern.

Figure 4. Primary Contaminants of Concern - Notified Events 2016



### Case Study: Portugal

The insured, a manufacturer and supplier of electrical power cables, had an incident resulting from an overflow of lubricants from its storage containers contaminating the adjacent special designation nature park and river. The insured was mandated by the regulatory authorities to clean-up the impacted areas and restore the damage caused to plant life at the park. Prompt mitigation measures were implemented, followed by active remediation. This resulted in satisfactory closure of the matter with the regulators .

Pollution emanating from fire fighting activities at waste and recycling sites has been an issue in recent years, due to the flammable nature of materials collected and stored at such facilities. In the UK, figures from the Chief Fire Officers Association show there have been around 250 incidents per year over the past decade. While firefighters work hard to try to contain run-off, their main priority with any fire is to prevent its spread and avoid any loss of life.

Pollution resulting from fires is an increasingly common trigger for notified incidents, according to Peter Jarvis, Head of Environmental Product, Europe, at AIG. Particularly as the scope of EIL coverage becomes better understood. "We've had an increased number of claims related to fire run-off and my gut instinct is we're going to see more fire-related incidents in the future," says Jarvis.

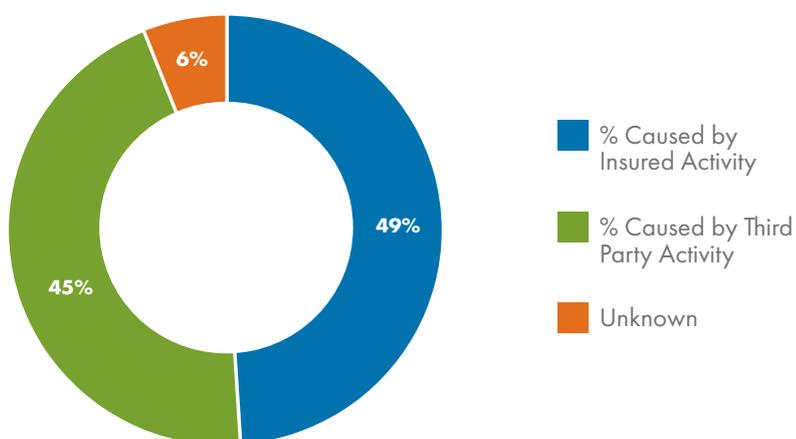
"Fuels and oil are always going to be up there when it comes to contaminants of concern, but we're starting to see claims on a much broader spectrum," he continues. "That goes back to buyers being more educated and triggering the policy."

### Why the polluter doesn't always pay

Regular purchasers of EIL insurance have developed a deeper understanding of the product and what it encompasses. "We're seeing greater use of the policy – which is good – and we are seeing claims and notified events which we haven't seen before," says Jarvis. "The types of incident haven't necessarily changed, but the mindset in the market has changed and there is a better awareness."

Insureds are also becoming aware they could be held responsible for the remediation costs of pollution or environmental damage caused by a third party. Jarvis notes this has been an issue for some of AIG's real estate clients where tenants responsible for historical cases of pollution cannot be identified. "We've had pollution claims that have fallen back onto the real estate property owners because the tenants became insolvent and disappeared. Thankfully they were insured."

Figure 5: Proportion of Claims caused by Third Party Activities



### Case Study: Italy

The insured, a manufacturer and distributor of electricity and gas, had a spill of approximately 168 million cubic metres of fuel from its service tank due to a malfunction of the level sensor switch. A crack in the secondary containment and separation wall allowed the fuel to migrate off-site, impacting the adjoining third-party property.

"It's definitely built into the environmental legislation that the polluter pays, but in the absence of the polluter being identified, the liability is likely to fall to the owner of the current site," he continues. "This is particularly the case in the UK. Very few authorities have the money to pay for the clean-up of major events and so they will pursue the liable parties."

Environmental losses are generally addressed under the following two types of law:

1. Compliance laws that regulate the day-to-day operations of the insured to avoid pollution; and
2. Civil liabilities laws that determine who pays for the consequences of pollution when it occurs. Actions under the civil liabilities can be brought by regulators as well as third parties that have suffered property damage, bodily injury or nuisance as a result of the pollution event.

"With environmental losses, very frequently compliance and liability are interconnected," says Mileidy Perez, VP Major Loss Environmental Claims Europe, AIG. "In our experience, far from becoming less stringent, we can see that the regulators are actually gaining more experience and comfort in the pursuit and prosecution of polluters following environmental losses."

While regulatory fines and penalties are not covered by EIL insurance policies, some insurers are providing added services to help clients avoid hefty fines by supporting risk management and prevention plans to avoid environmental accidents occurring in the first place.

"In many cases, sentencing proportionate to the insured's financial resources could result in a significant fine," says Perez. "Liability can be assessed against direct polluters, and knowing permittees of pollution. Operators can also be liable for environmental damage caused to third parties, even when operating within permit limits."

"As a consequence there is a growing necessity for insureds to be mindful of the scope of their operations, the status of the land they are operating on and an appreciation that it is not always just the polluter who pays," she adds. "If the regulators cannot find who caused the incident they could still go after an insured if the damage or pollution is on, or is emanating from, their property."

This has proved to be a wake-up call for many of the brokers and risk managers. "In light of Brexit, insureds and brokers have asked us whether we think UK regulators are going to be less stringent" adds Perez. "While we do not have a crystal ball, we do not foresee an incentive to change environmental laws that work merely because they were derived from the EU."

"We further note that regulators in the UK often pursue actions under domestic UK environmental laws that are not rooted in EU legislation, such as the contaminated land regime Part 2A of the Environmental Act 1990, and that third-party claims are often brought under domestic common law liability," she concludes. "As such, we do not expect regulators and third-party actions to decrease in the UK in future."

### Case Study: Spain

The insured, the owner and operator of a thermo electric solar plant, caused a discharge of thermal fluid due to a ruptured pipe, requiring clean-up of soil impacted off-site by the regulatory authorities.

## Key environmental questions companies should be asking

- Do you understand the full extent of your environmental liabilities?
- Are you clear what support is available to help you prevent environmental incidents from occurring?
- What measures has your organisation put in place to protect you against your environmental liabilities?
- Does your insurer offer local specialised environmental expertise?

### Methodology

For AIG's 2016 environmental claims insights, data was collated on 126 notified events from AIG's European Commercial Industrial insured's across EU member states including: Belgium, Denmark, France, Germany, Ireland, Italy, Portugal, Spain, Sweden, and the United Kingdom. The notified events include major corporate and Small to Medium Size Enterprises (SME), incorporating a wide range of sector activities.

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