



environmental protection, a new element in the development of insurance business

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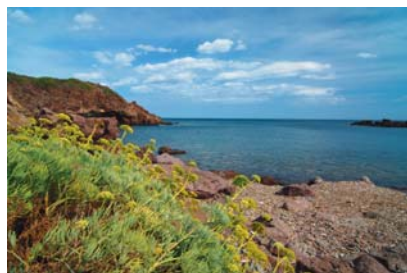
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On the principal of “whoever pollutes pays”, Spanish environmental legislation includes the need to recover possible damage or avoid situations of imminent risk to the environment which occur as a result of carrying out economic activities.



Environmental liability

Due to the transposition of the new EU framework on environmental liability, established by Directive 2004/35/CE, into Spanish legislation, Law 26/2007 of 23rd October on Environmental Liability (Official State Bulletin No. 255 of 24/10/2007) has been incorporated into the Spanish Constitution.

This law is in line with the principles of Sustainable Development (laid down by the 1987 United Nations World Commission for the Development of the Environment) and supplements the specific regulatory development to protect, maintain and preserve the environment against possible deterioration in its quality caused by humans in the pursuit of economic activities.

The Environmental Liability Law strengthens the regulatory references which are already present in Spanish legislation, in this regard, such as Article 45 of the Constitution, in that it expressly recognises the need to repair the damage occasioned to nature and natural resources, regardless of any administrative or criminal sanctions which may apply.

25% of Spanish territory is affected by some aspect of protection, hence the importance of this new law.

The area of application of the law includes damage to water, soil, the coastline, rivers, and damage to species of wild flora and fauna permanently or

temporarily present in Spain, as well as damage to the habitats of all indigenous wild species. The latter is particularly relevant if we bear in mind that 25% of Spain is protected and this includes more than 1,000 areas split among the various Autonomous Communities.

To avoid duplication with other liability regimes regulated by other laws, such as public liability, injury to persons and damage to their property are excluded from the area of application of the law, except where they constitute a natural resource.

The main new aspect that this law provides is recognition of an unlimited liability with regard to damage occasioned to the environment, in order to restore it to the condition it was in before the disturbance that caused the damage, with an obligation to bear the total cost associated with the preventive and repair work required to achieve that objective.

Generally speaking, the law affects all operators who pursue an economic activity in Spain and who could damage the environment. In addition, in some cases, it specifically establishes an objective liability regime in which the obligations of the affected operator are imposed regardless of any blame, deceit or negligence which may have existed in his behaviour.

In any case, the objective liability falls on the activities mentioned in Appendix III of the law (see Table 1), and on other activities only if they produce threats of imminent damage in the opinion of the competent administration.

Table 1. Principal activities included in Appendix III of Law 26/2007

Activitie	Affected installations	
	Number of affected installations	% ot total number of installations
Combustion installations	143	0.2
Metal processing and production	583	1
Mineral industries	699	1.1
Chemical industries	436	0.7
Paper and board industry	112	0.2
Farming and livestock industry	2,690	4.4
Textile and leather industry	44	0.1
Promoters and major producers	5,000	8.2
Waste. Waste water purifiers	17,199	28.1
Manufacture, storage, processing and bottling of dangerous substances, phytosanitary and biocidal products	3,371	5.5
Transport	30,000	49
Management of waste from extraction industries	988	1.6
Total	61,265	100

Produced by ITSEMAP from an analysis of Appendix III and data supplied by the Department of the Environment.

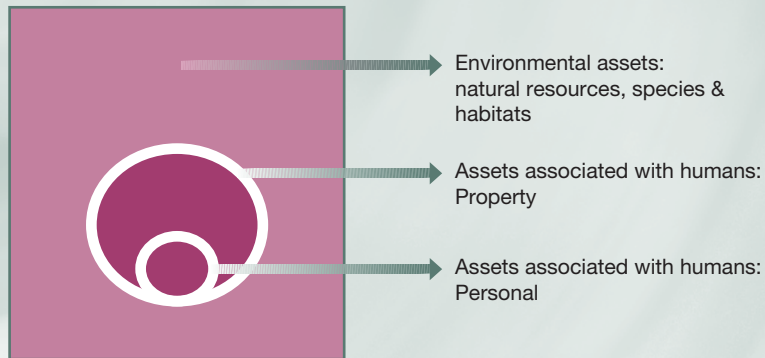
The obligation to set up a financial guarantee to cover possible environmental liability does not come into force until 2010.

The activities included in Appendix III must, as an essential requirement for their development, set up a financial guarantee to partially cover their environmental liabilities, so that the operator can have adequate economic resources. This may take three forms: insurance, a guarantee from a financial institution authorised in Spain or setting up a technical reserve specifically for this purpose. However, this obligation, which will be established by the gradual approval of Ministerial Orders at sector level, will not come into force until 2010.

Regulation 2090/2008 introduced by the law, establishes the compulsory nature of carrying out an analysis of environmental risks for those activities included in Appendix III of the law, in order to be able to establish the size of the financial guarantee for each type of activity, according to the intensity and extent of the damage that could be occasioned. The reference methodology for risk assessment is UNE standard 150008 on environmental risk assessment supplemented by the monetisation of the risk, in other words, assigning an economic cost to the identified environmental risks. Under no circumstances may the said compulsory figure be more than EUR 20 million.

This means that insurance companies may be able to market new products which include environmental liability. The inclusion of this environmental insurance in traditional insurance product portfolios means a challenge, as well as an opportunity (Chart 1) which requires investigation and the definition of various key aspects for proper interaction between the environment and insurance business.

We can call on previous experience for this. In Spain, we have been marketing environment related insurance products connected with public liability for contamination, cover which is required by waste sector legislation Law 10/98 on waste and Royal Decree 833/88 which regulates the handling of dangerous waste.


Chart 1. Changes in the scope of insurance cover


The amount of premiums associated with public liability insurance for contamination in Spain in 2006 was EUR 5.5 million, a much lower figure than in other markets, such as for example the United Kingdom, where premium volume reached approximately EUR 50 million 2004. This fact, together with the experience acquired in more developed markets, such as the United States, which has gone through various phases to reach its current maturity with an estimated total premium volume of about USD 1,500 million in 2004, heralds substantial development in this market in our country.

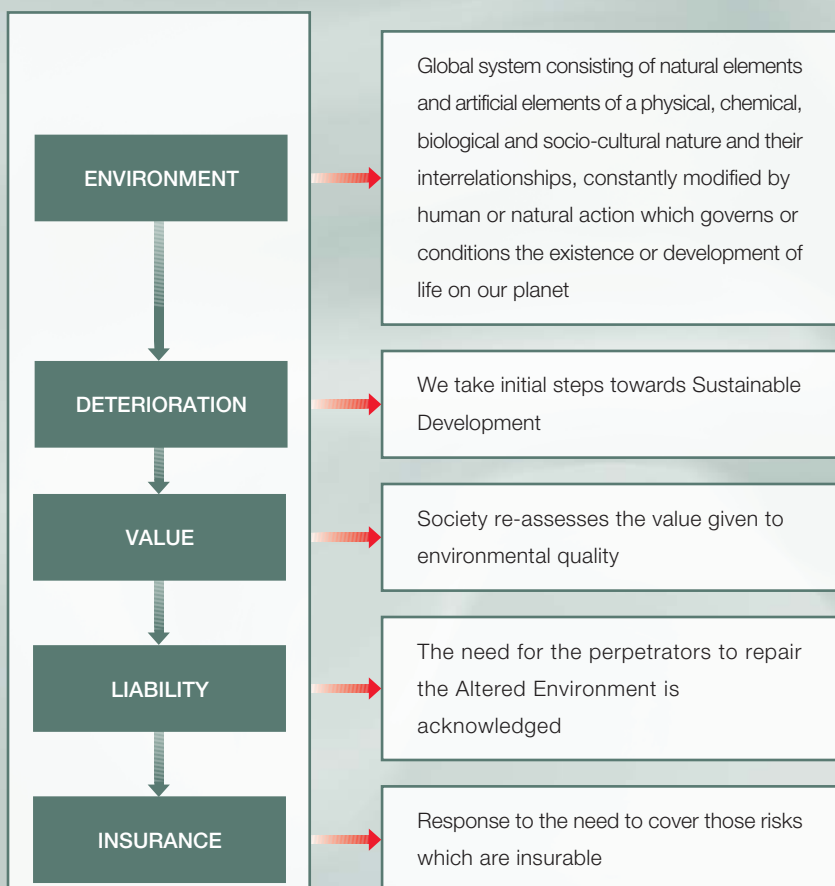
Current compulsory insurance (for example, for developers and producers of dangerous waste) must be adapted to the new reparation obligations established in this law, and therefore it will be affected by this change and cover will be improved with the new products.

The Environmental Liability Law establishes a new type of administrative liability, in addition to the public liability for contamination that already exists in Spain, and so new cover requirements are generated to which the current insurance offer does not provide an adequate response.

The insurance offer

MAPFRE EMPRESAS has developed Multi Risk Environmental Insurance and Supplementary Modules to encompass the liabilities which have been insured until now and those brought about by the new law, insofar as they are insurable, in a single policy.

Some of the preliminary technical questions associated with these products to be taken into account are detailed below:

Chart 2. Principal factors in the process of insuring the environment




1. LIABILITY. There can be two types of claims for one and the same cause:

■ Environmental liability is the one that will be required by the competent administration in order to repair *environmental damage*.

■ Public liability for contamination is liability for injury to persons, damage to property and financial losses due to contamination.

2. ENVIRONMENTAL DAMAGE are those to natural resources, specifically wild species and their habitats, water, coastline, rivers and soil.

3. INSURED'S OBLIGATIONS:

■ To anticipate imminent damage.

■ To minimise any damage already caused.

■ To repair the damage.

4. REPARATION OF ENVIRONMENTAL DAMAGE

■ Primary reparation - The damaged asset must be repaired, insofar as it is viable.

■ Supplementary reparation - In addition, other action must be taken to compensate for any damage remaining after the primary reparation.

■ Compensatory reparation - Finally, some other type of action must be taken to compensate for loss of enjoyment of the natural resources during the time they were damaged.

None of these actions consists of financial compensation to third parties.

Content of cover

Module A is the basic cover and B and C are additional and optional.

Module A): Environmental liability for contamination

■ Type of insurable damage: **Cover will be limited to damage due to contamination**, excluding other types of possible environmental damage (fire, illegal felling or hunting, etc.)

■ Insured costs: Insures those aspects required as a minimum in the law for insurance which will eventually become compulsory; the supplementary and compensatory reparations described in Appendix II of the Law are also included with a limit of 10% of the sum insured of Module A). The cost of decontaminating the soil itself is excluded.



► **Incident:** For the cover to come into force, there needs to be an accidental incident generating the damage, regardless of whether its appearance was gradual or sudden, according to the circumstances or method of cover. An accidental incident which gives rise to an imminent risk of environmental damage is also considered to be a generating incident and the corresponding cover comes into force.

► **Moment of occurrence of the incident:** The temporal scope of the cover is determined by the first reliable discovery of the contamination or imminent risk of contamination.

Module B): Cost of decontaminating own soil

The specific benefits associated with this module relate to the **decontamination of the soil** of the insured property and other related costs.

This cover has been split into a separate module because taking out this cover will require additional information on the condition of the soil and specific risk assessment criteria will apply.

Module C): Public liability for contamination

The content of the cover is equivalent to that provided by current environmental cover for damages to third parties due to contamination, including so-called “Employer” cover, in other words, **accidental injuries occasioned to employees due to contamination.**

Sums insured

Two independent sums insured are established: one to cover environmental

liability and the other to cover public liability due to contamination; both can be exhausted simultaneously by one or more claims on the various modules. The accrued annual limit is also set separately for both modules.

As regards the cost of decontaminating the soil itself, on the other hand, there is no additional sum insured, the same amount as for environmental liability cover being set as the limit of indemnity, all claims declared under each cover contributing to exhausting the said limit.

Insured activities

Generally speaking, the new insurance is applicable to all economic activities, including the general risks of the insured

activity as well as other activities carried out by the insured, provided they can be considered as auxiliary activities (representatives, attendance at fairs, transfer of proprietary products).

Reducing the environmental risk in companies and organisations

There are significant direct and indirect implications for company management. According to the philosophy of the Environmental Liability Law, the aim is to create an environmental risk management culture within the company which enables operators to anticipate, assess and financially cover the environmental risks of their installations in order to protect the majority of the



elements making up the environment. All this has a dual objective: to avoid accidents which can affect the environment and have sufficient cover to respond to possible damage.

In this way, the assessment of the environmental risks of the installations and activities takes on double relevance. It thus becomes a keystone to be able to assume the new responsibilities with insurance cover. The strategy is to reduce the risk associated with the installations by means of a cost benefit analysis.

In view of the residual risk, there are two alternatives: keeping it within the company, assuming a possible loss, the recommendation being to set up a financial reserve to cover a claim or, transfer it to the insurance market by means of an insurance product.

In negotiating the conditions of the insurance, it is particularly relevant to set an adequate sum insured so that

there is no discrepancy between the valuation of the potential risk and its insurance cover. It should be remembered that the Environmental Liability Law does not limit liability to the financial cover and that even though the law rules the determination of a sum for the compulsory cover according to the environmental risk of the activity carried out, this is conceived as a minimum cover and under no circumstances limits the liability for assuming costs over and above that figure if they occur.

Having reduced and transferred the risks associated with an installation, there is one thing left to do, increase control over possible accidental emissions so that in the event of a spillage or leak, there are early detection systems which can reduce the response time and thus the costs associated with the damage.

Finally, it should be stressed that the organisation of human and material

resources to deal with environmental emergencies must be integrated into the activity by means of the company's self-protection plan. This involves carrying out specific procedures on the actual installation thus preventing standard procedures from being shown to be ineffective in the event of a risk.

Management of accidental situations and recovery of the damaged environment

Unfortunately, accidents happen even though adequate risk management has been carried out, in which case organisations must seek expert advice from professionals to limit the damage caused and define a speedy and efficient plan of action.

There is currently no complete source of data relating to incidents with consequences on the environment, with sufficient guarantees of providing





reliable data. It is therefore difficult to ascertain the frequency of this type of event. As an alternative it is possible to use data available from various sources. This has enabled the annual number of accidents involving damage to the environment to be estimated at about 76 accidental events in fixed installations and 60 in transport.

Neither are there comprehensive references as to the costs associated with these incidents, except in the case of major incidents such as Aznalcollar in Doñana (Seville, Spain) which could be classified as major, where the recovery costs exceed EUR 100 million. By establishing various working theories, it has been estimated that the average cost associated with occurrences in fixed installations, such as spillages when discharging waste tanks, or a fire in an industrial plant, could be significantly lower than that figure. ■

Table 2. Main damage covered by public and environmental liability

Public Liability	Environmental Liability
Damage to property of individuals	Damage to water bodies
Damage to the property of public institutions	Damage to protected species and habitats
Financial losses or loss of personal rights	

Table 3. Main differences in the application of the Public and Environmental Liability regimes

Public Liability	Environmental Liability
Injured third party	Competent administration
Civil claim	Administrative act
Judicial decision	Power of self-guardianship
Compensation or reparation by judicial or extra judicial agreement	Prevention and reparation measures

