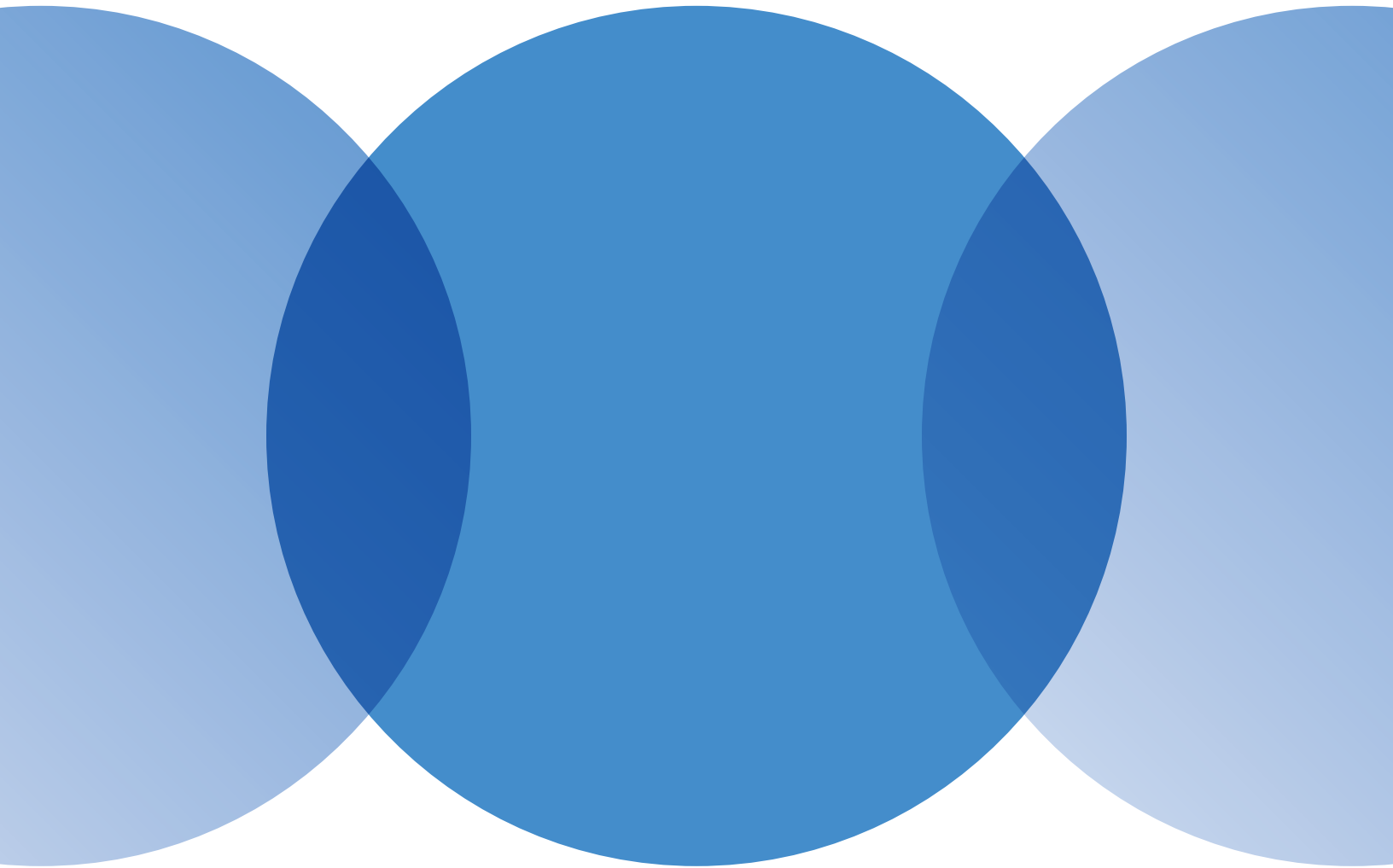


# Environmental Risk Management Strategies for a Changing Environment



This paper focuses on specific preparations companies may take to address the risks and costs of potential future environmental claims events. It offers some practical risk management strategies that could serve to minimize the severity and cost associated with such claims.<sup>1</sup> Such risk preparedness measures include process re-engineering; emergency response and overall contingency planning for spills and accidents; e-discovery preparedness; and compliance with government regulations on reporting and for keeping adequate records, including new government greenhouse gas reporting requirements.<sup>2</sup>

Generally speaking, environmental risks are analyzed by understanding federal, state and local environmental regulatory requirements and enforcement developments; loss history and trends; standards of best practice for a particular industry operation or exposure; scientific and technical information; and society's attitudes, including third party claim or litigation trends. In the case of environmental risk, many of these factors will change over time, and therefore to be effective risk management must be a fluid process that keeps up with the latest risks and trends. Process re-engineering, emergency response planning, and greenhouse gas regulation are good examples of this fluid process.

### Process Re-Engineering to Minimize Environmental, Health and Safety Risks

Over the past twenty-five years, leading companies in a number of industries around the world have recognized that they needed to undertake voluntary process re-engineering to minimize environmental, health and safety risks related to their businesses. There are a variety of different approaches to process re-engineering, including: development of tightly controlled and limited emissions systems for industrial processes, or even closed-loop systems; limiting energy and materials process inputs or substitution of sustainable or "environmentally less costly" materials for traditional production materials; and development of sustainable supply chain systems and packaging. Notably, in some cases re-engineering efforts have involved risks that were not presently regulated because companies anticipated that in the future they might be regulated. Despite the numerous advances made by companies in this area, it seems likely that more re-engineering can profitably be done to enhance company environmental competitiveness, especially by minimizing future claims liabilities for worker and public health and environmental damage.

In short, thoughtful process re-engineering should be an integral part of a company's efforts to minimize its environmental, health and safety risks. Similarly, forward-looking U.S. and European companies have often tried to conduct their operations around the globe voluntarily using uniform higher standards than host countries may have required. They did so because they recognized that such actions may avoid future liability claims, even in countries that have traditionally had loose standards, since those may change.

<sup>1</sup> Risk management is the identification, assessment, and prioritization of risks (*the effect of uncertainty on objectives*, whether positive or negative) and acting in such a manner, or prescribing policies and procedures, so as to avoid or minimize loss associated with such risk. International Standards Organization (ISO) 31000:2009, published 13th of November 2009. ISO 31000 provides risk management principles and guidelines and is one of many tools generally available when designing a risk management strategy. The strategies to manage risk include avoiding the risk by not participating in the activity; accepting all of the consequences of a particular risk; reducing negative effects of risk by implementing risk mitigation methods; and/or the transfer of risk to another party via written contract including a private party insurer or guarantor.

<sup>2</sup>In the past we have provided our insight into claim trends – the types of claims that have emerged or that could potentially emerge around specific chemicals of interest or industry operations and the potential health and environmental effects of exposure to such chemicals and operations; litigation trends for natural resource damages; environmental agency remediation re-openers of closed claims; and potential legislation on the horizon concerning, for example, greenhouse gases (GHG). See White Paper, Environmental Claims: What's Old, What's New, What's Coming.



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## Emergency Response and Contingency Planning

An emergency response will generally be required when there is a release of oil, radioactive materials, hazardous chemicals or other regulated substances into the air, land, or water that threatens public health or damage to the environment.

Typically, these events pose sudden and immediate threats or dangers and trigger legal duties for: (1) timely reporting of the event to federal, state and local environmental authorities with jurisdiction over it<sup>3</sup>, (2) containing and abating the release event if ongoing, and (3) responding to damage or potential threats of damage. Emergency events can stem from various causes including: (1) transportation accidents; (2) events at facilities that generate, use, store or dispose of chemicals and other materials; (3) operator or contractor negligence in performing work or services; or (4) natural or human-caused disaster events.

To minimize harm from an environmental accident and maximize the effectiveness of emergency response, companies should have in place an emergency preparedness plan that can be implemented at the time of the event and will coordinate its contacts and action according to such a plan. The plan should include essential contacts for response including emergency response contractors in the vicinity of the affected location or locale of business operation. As an example, the Spill Prevention, Control, and Countermeasure (SPCC) Plan (for oil spill prevention, preparedness, and response to prevent oil discharges to navigable waters and adjoining shorelines) includes a section that integrates all of these elements.<sup>4</sup> An effective emergency response can serve to minimize the size of releases to the environment, reduce potential damage and required cleanup response, and avoid or mitigate third party claim activity or fines and penalties.

Environmental response planning is typically an essential part of overall company emergency contingency planning. Consideration should be given to creation of one contingency plan covering all aspects of response, taking into account the complexity of the release event. Environmental agencies are usually responsible for establishing and enforcing environmental standards associated with an emergency release event including reporting, containing and abating, and cleanup and/or response activity. However, environmental agencies often will not have the authority to effect evacuations, rescue, crowd control, or other emergency services that may be required. Public services and civil authorities may have distinct safety and public health concerns, such as sealing off locations and aiding any injured parties. Moreover, issues involving interacting with the media; employee, client, or vendor notification; and relocation of business operations are specific to individual businesses and should be included as part of a contingency plan. An effective contingency plan will consider the interactions among environmental agencies (federal and state depending on the release event), public services, civil authorities, and private company partnerships.

One important lesson for businesses from decades of public environmental concern is that how effectively a business responds to an emergency situation like a release of hazardous materials can have lasting effects on its reputation, and on the future level of regulation it faces from state and federal governments. The Bhopal disaster in India, for example, had repercussions in the U.S. and India for more than two decades. Careful emergency response planning and contingency planning can therefore offer powerful advantages for protecting a business's overall image and sustainability through a release event crisis.

<sup>3</sup> Most releases of this type are to be reported through or direction for reporting given through the clearing house via US EPA at National Response Center at: 1-800-424-8802. See <http://www.epa.gov/epahome/violations.htm>

<sup>4</sup> <http://www.epa.gov/oswer01/content/spcc/index.htm>

## E-Discovery Preparedness

Many businesses have learned important lessons on best practices in electronic discovery management the hard way – after an event has occurred, litigation ensues and information must be collected, processed, reviewed and produced to opposing parties and courts of law at very large cost.

E-discovery demands and litigation-mandated responses are unavoidable and are fast becoming the state of the art discovery method in litigation. This is especially true when—as is often the case in environmental, health and safety matters—the relevant facts for the determination of liability call into question past company operations, complex procedures, or the development and testing of company products.

When put in place prior to a release event, an e-discovery preparedness plan can assist any size business operation in collecting litigation discovery responses, responding to information demands, and cutting costs of discovery response substantially. An e-discovery plan will typically involve taking an inventory of documents relevant to any businesses' operation and/or specific lines of business. Once the business has taken stock of the information available electronically and in paper format, a document review strategy and a plan of retrieval are designed to be implemented in responding to a future e-discovery request. Another issue to be considered in the planning process is the flexibility to respond to diverse parties with different claims, such as government information demands. And such plans must be integrated with state and federal document retention requirements.

Federal and state laws impose document retention requirements of varying lengths and scope on different types of companies and different parts of their operations. An obvious example is tax-related records; but increasingly, company records of other kinds, including various environmental records, are the subject of such retention requirements. Wholly independent of retention requirements, the beginning of litigation often gives rise to a company's separate duty to preserve evidence—whether in hard copy or electronic form—which courts will enforce in the discovery process. Failure to observe such records requirements or evidence preservation obligations is typically subject to substantial penalties, and, in some cases, could be deemed by a court to create a presumption against the company with respect to its liability.<sup>5</sup> In the worst case, failure to preserve evidence or produce discovery could lead to the court's dismissal of important company claims or defenses. In short, violations of record retention or document preservation obligations can potentially be exceptionally damaging. One important aspect of company preparation for discovery and potential claims is to understand what kinds of records it must retain and deciding what kinds of records it will routinely retain for what periods of time, and how it will preserve evidence during litigation.

## New GHG Reporting Rules and Recordkeeping

EPA's Mandatory Greenhouse Gas (GHG) Reporting Rule requires reporting of GHG emissions from large sources and suppliers in the United States.<sup>6</sup> This rule is intended to inform future policy decisions and programs to reduce GHG emissions. The data will also allow businesses to track their own emissions, compare them to similar facilities, and identify cost-effective ways to reduce their emissions in the future (through process re-engineering or trading, for example). Under this rule, suppliers of fossil fuels or industrial greenhouse gases, manufacturers of vehicles and engines, and facilities that emit 25,000 metric tons or more per year of carbon dioxide equivalent (CO<sub>2</sub>e) are required to submit annual reports to EPA regarding their emissions. EPA's GHG reporting requirements require that company officials certify reports based on proper monitoring and calculations. Statutory Clean Air Act penalties may be imposed for failure to comply with the reporting requirements.

<sup>5</sup> A leading recent case on this subject is *Pension Committee of University of Montreal v. Banc of America Securities, LLC.*, No. 05 Civ 9016, 2010 Westlaw 184312 (SDNY Jan. 15, 2010).

<sup>6</sup> 40 CFR Part 98 was published in the Federal Register ([www.regulations.gov](http://www.regulations.gov)) on October 30, 2009 under Docket ID No. EPA-HQ-OAR-2008-0508-2278. Part 98 became effective December 29, 2009.

On April 12, 2010, EPA issued four new proposed rules that amend the GHG rule. These proposals would require reporting of emissions data from the oil and natural gas industry segment, industries that emit fluorinated greenhouse gases, and from facilities that inject and store carbon dioxide (CO<sub>2</sub>) underground for the purposes of geologic sequestration or enhanced oil and gas recovery. In addition, EPA proposed to add three new reporting requirements to the General Provisions of the rule.<sup>7</sup> On June 28, 2010, EPA issued a final Mandatory Reporting of Greenhouse Gases rule for four additional source categories: Magnesium Production, Underground Coal Mines, Industrial Wastewater Treatment, and Industrial Waste Landfills.

Businesses and facilities should determine if they are subject to the GHG rule and take necessary steps to develop appropriate GHG monitoring and reporting plans and if necessary, install required equipment, and/or maintain monitoring equipment, collect GHG monitoring data, and prepare GHG reports for submission to EPA. At this time, it is not possible to predict with any certainty to what extent EPA will expand the scope of its GHG monitoring and reporting requirements beyond present levels, but it is possible that the scope of these requirements will be expanded during the next few years—which reinforces the importance of process re-engineering as an integral part of environmental risk management.

### **Conclusion**

An important element of every risk management program, after appropriate and necessary risk mitigation and preparedness programs are in place, is to consider how the business is prepared to deal with a possible future claim or loss, regardless of risk mitigation efforts. A casualty insurance program, including environmental insurance, can complement quality risk management programs and will operate best when the insured has taken all reasonable steps to control risk, thereby leaving insurance for protection against fortuitous and catastrophic losses.

<sup>7</sup> In May and July 2010, EPA also proposed rules that include technical corrections and clarifying and other amendments to the original reporting rule. See <http://www.epa.gov/climatechange/emissions/proposedrule.html> for more information on these proposed changes and technical corrections. EPA plans to finalize these proposals this year, and has stated its intent that they would become effective in 2011.

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