

Unlocking the potential

Environmental insurance These policies are not new, but they may be the key to accessing lucrative developments. Doug Bryden discusses the options

Environmental insurance can be the key that unlocks potentially lucrative but environmentally sensitive transactions and developments. Although not a panacea, the right environmental insurance is increasingly helpful in managing environmental risks (real or perceived) and allowing parties to overcome deadlocks.

Soil and groundwater contamination continues to be a potentially material danger. However, developers, landowners and site operators have become more familiar with such risks. It is now common for parties to take a view or to seek comfort from an often limited contractual recourse against parties with weak or no covenant strength.

The UK's contaminated land regime has never been particularly effective. However, a number of cases, such as *Corby Group Litigation v Corby Borough Council* [2009] EWHC 1944 (TCC); [2009] PLSCS 236, together with new legislation, including the Environmental Liability Directive, highlight how an overly relaxed approach to environmental risks could leave parties with significant liabilities. These, alongside more risk-adverse market conditions, mean that sustainable and robust liability management solutions should be sought where possible.

What is available?

● **Public liability insurance (PLI):** Certain environmental risks would historically have been covered by more general PLI policies. However, as the scope and magnitude of environmental liabilities became increasingly evident in the 1970s and 1980s, these risks were expressly excluded from PLI policies.

The Association of British Insurers' standard environmental exclusion wording, which restricts cover to third-party damages arising from a "sudden, unintended and unexpected" pollution incident, is widely used in PLI policies. Thus, the cover offered has potentially significant gaps: for instance, losses arising from gradual pollution, which is the usual source of issues surrounding material soil and groundwater contamination.

The problem is exacerbated by the strict approach of the courts when interpreting the wording of insurance policies relating to pollution and contamination liabilities.

In *Bartoline Ltd v Royal & Sun Alliance Insurance plc* [2006] EWHC 3598 (QB); [2007] 1 All ER (Comm) 1043, it was held that a policy covering damages did not cover liabilities for the cost of remediation imposed under statutory remediation notices. Such limitations have given rise to bespoke environmental insurance products.

● **Environmental impairment liability (EIL):** EIL policies (or pollution legal liability policies) are perhaps the most common form of environmental insurance used in affected transactions. The policies, which run for up to 10 years, aim to plug the gaps in PLI insurance and provide cover for losses arising from historical pollution or contamination. Adequate information on the past use and environmental setting of the subject site is required before an EIL policy can be obtained. If the site has had a significant industrial history or involves complex environmental issues, it may be necessary to carry out intrusive surveys.

These policies do not cover all soil and groundwater risks. They generally exclude or restrict losses arising from existing pollution conditions that are subject to regulatory action or third-party litigation or where such action is "reasonably foreseeable". In some cases, it is possible to obtain cover for known pollution where the liabilities are not reasonably foreseeable and the action is "fortuitous". However, such wording will usually require a detailed understanding of the site as well as lengthy negotiations.

EIL policies will normally exclude the clean-up costs required to develop a site to a more sensitive use and contamination caused by ongoing operations.

● **Operational risk (OR):** OR policies cover liabilities associated with contaminative events occurring after the date on which the policy begins. They are used more for the management of environmental risks than in transactions. However, where an owner or occupier has built up a significant "tail" of OR cover, this can be a powerful tool in de-risking environmental issues in any future divestment. It will be necessary to take steps to ensure that the benefit of the policy passes to any future purchaser and covers the requisite period.

● **Remediation cost cap:** This seeks to cover any unexpected and/or spiralling

costs that arise during the remediation of known contamination. The contamination can often be more extensive or significant than was originally anticipated. These policies help to mitigate such uncertainties and ensure a more effective use of capital funds. However, they are suitable only for significant projects with a remediation budget of more than £2m and can be costly as well as subject to deductibles or co-insurance structures.

● **Contractor pollution liability (CPL):** CPL policies cover contractors against contamination liabilities that may arise during the provision of their services. Although generally forward-looking, they can be retrospective (an insurer will require a significant degree of information before offering such cover). They often bolster the limited comfort provided by a contractor's professional indemnity insurance.

Recent developments

● **Risk screening products:** These supplement high-level environmental desktop reports and offer limited cover, in terms of duration and amount, and apply only to lower-risk sites. They are attractive to risk-averse purchasers of offices and other commercial properties, especially where detailed on-site investigations are not practicable or appropriate contractual protection is not available.

● **Liability buyout:** Insurance providers and technical consultancies now offer liability buy-out products designed specifically for the UK and European markets. These aim to take environmental issues away from the buyer and seller and to transfer risks to an unrelated third-party specialist by way of a hybrid of indemnities and insurance.

● **Insurance archaeology and recovery:** Innovative lawyers, brokers and technical specialists continue to develop services that seek to deal with environmental issues via old policies. Insurance archaeology, which aims to reconstruct and analyse historical policies to de-risk environmental issues, has proved to be a cost-effective solution.

As well as offering an effective vendor due diligence tool, the researching of old policies may also allow for the recovery of costs and other losses arising from historical contamination and pollution. However, this will require careful legal and technical analysis.

Environmental insurance is not new. However, with underwriters showing a renewed appetite for such policies, the availability of a broader range of products and the inadequacy of more traditional liability management mechanisms, environmental insurance may be just the thing to unlock that tricky deal.

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