

1st Climate Change Summit for Asia's Insurance Industry Singapore 16-18 January 2011

**Legislating for Change: What new laws or
liability issues should be of greatest concern for
insurers?**

A review from around the globe

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“Climate change is an issue of justice as much as of economic development”

Gordon Brown, while UK Chancellor, at G8 meeting of environment and development ministers, 15 March 2005

“You get justice in the next world: in this world you have the law”

William Gaddis, *A Frolic of His Own*

- Taken from *“The Finance of Climate Change”*- Chap 29 Myles Allen *“The Spectre of Liability”*

Legislating for Change: What new laws or liability issues should be of greatest concern for insurers?

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OUTLINE

1. Introduction
2. AIDA Climate Change Working Party
3. Impact of Climate Change on existing insurance lines
4. Applying defensive measures
5. Definition of risk and identification of cause
6. Liability issues
7. New liabilities, new products, new challenges
8. The Forecast?

1. Introduction

1. **Physical effect:** Climate change → weather patterns more variable + severe weather events more frequent/intense
2. **Insurance impact:** Most traditional insurance classes: property, liability, personal
3. **Defensive steps:** Many taken by (re)insurers worldwide in response. Policy and underwriting provisions/measures. “Green” initiatives/exploration of new products for new exposures.
4. **Legislative/liability climate:** Awareness needed of fast-changing landscape of regulation, legislation and rulings about liability around the world: at local, national, regional + international levels.
5. **Keeping up:** How possible or best to keep abreast of so much legislative and political change and uncertainty responding to/anticipating the effects of Climate Change?

2. AIDA Climate Change Working Party

“Climate Change and Insurance Law” / AIDA Climate Change Working Party

- AIDA XIIIth World Congress Paris, May 2010
- Responses to Questionnaire
 - Local context, inc. legislation /regulation
 - Impact upon insurers – lines affected/definition of risks/insurers’ protective measures to minimise exposure/new products
 - Role of reinsurance/ART
 - Co-operation/competition with public sector responses
- Identification/Discussion of Major Themes
- Final Report - Prof Marcel Fontaine
- Creation of AIDA Climate Change Working Party

3. Impact of Climate Change upon existing insurance lines: (1) Property Risks

PROPERTY RISK TYPE	POTENTIAL HIGH-HAZARD RISKS (DEPENDING UPON LOCATION)
AGRICULTURAL INSURANCE	Damage to crops, forestry, livestock
BUILDINGS, CONTENTS, MOBILE HOMES, MACHINERY/EQUIPMENT	Natural perils + related risks of subsidence etc
TRANSPORT AND MARINE	Loss of equipment, transported /stored goods, supply chain/delivery risks
TOURISM/LEISURE SECTORS	Disruption to holiday/leisure facilities
EXPORT CREDIT/POLITICAL RISKS	Resources disruption → more disturbances/conflicts
BUSINESS INTERRUPTION	Across all sectors
NEW ENERGY SOURCE RISKS	Windmills, wind farms, solar power

3. Impact of Climate Change upon existing insurance lines: (2) Liability Risks

LIABILITY CLASS	POTENTIAL HIGH-HAZARD RISKS (DEPENDING UPON LOCATION)
Public	Health care, Transport, those served in coastal zones/flood plains/affected locales
D&O	All of above, Energy, Metals/Mining, Construction materials, Water, Insurance, Public agencies, Asset/Property management
Products	Food & drink, Construction materials, clients with supply chains exposed to developing country/hazardous locale increased risks (coastal, flood plains etc)
Employers	Agriculture/Forestry, Construction
Professional Indemnity	Construction, many professions, financial and even insurance advisers

3. Impact of Climate Change upon existing insurance lines: (3) Personal insurances

TYPE	POTENTIAL HIGH-RISK AREAS
Life	Mortality rates may become radically altered over time by geographical area and effects of severe weather events (inc. heatwaves) and related phenomena life-threatening/injurious to health
Health	Changed/potentially raised exposures for regions/individuals to disease, malnutrition, cancers, stress etc
Income /mortgage protection	As above

4. Applying defensive measures

- **Forms:**
 - Knowledge-gathering/re-modelling; encouraging improved risk management; policy/underwriting adjustments to protect results.
- **Intending legal effect:**
 - Stricter conditions/sanctions imposed to avoid/mitigate loss
 - Premium adjustment
 - Incentive of reduced premiums if good practices adopted
 - Imposition of coverage caps, restrictions on/exclusions from defined risks covered
 - Cancellation/withdrawal of cover/from market
 - Co-insurance/reinsurance dependence to offset higher exposures
 - Reliance upon/resistance/submission to public/compulsory schemes for certain risks
- **Legal context:**
 - Local laws governing liability and insurance coverage issues + more specific Climate Change legislation/initiatives - both may impact upon availability/effectiveness of many measures.
 - Particular concern: (i) precise **definition of risk** (and exclusions); and (ii) in event of loss, **identification of any cause**.

5. Definition of risk / identification of cause (1)

Problems of defining “Climate Change” risk + identifying critical cause of any “Climate Change-induced” loss derive from same source.

(i) Definition of risk /of “Climate Change”

- Climate Change - not of itself *new* (insured) risk, but what *aggravates existing* ones.
- Storms, environmental liabilities, malaria: none = new phenomenon. Insurers long happy to cover losses from each.
- Insurers want protection from increase of risk induced by Climate Change, but how restrict /exclude *increase* alone?
- Existing pollution exclusions *may not* suffice to exclude all liabilities involving some GHGs , eg CO2.
- Monetary caps /limits probably easier. Problem with exclusions /descriptions of risk = not to cast doubt upon elements of cover intended to remain covered/excluded. Task made harder by the absence of many statutory definitions of CC. More may arrive in due course and should be considered.
 - World Meteorological Organisation (WMO) defines “Climate” as “*average weather*”, variability of which generally measured over period of approx. 30 years.
 - UNFCCC definition of “Climate Change”:
‘... a change of climate which is attributed directly or indirectly to human activity that alters the composition of the global atmosphere and which is in addition to natural climate variability observed over comparable time periods...’

5. Definition of risk / identification of cause (2)

(ii) Identifying *the* cause

- Invariably a *combination* of causes.
- On balance of probabilities science likely to show CC *was* responsible for (or at least contributed to) increased severity/likelihood of damaging weather (or CC-related) event
- BUT underwriter/contract draftsman/courts must still consider:
 - what if one of contributing losses was quite *separate* human failure, e.g. the failure of the local authority to maintain /adjust sewage system/build adequate flood defences or failure of company to (do no more than) meet minimum standards?
- Failings on part of policyholder may as usual trigger insurance law rules on the risk of aggravation, breach of policy conditions + so potential forfeiture of cover.
- What if an insurer on risk for one contributing cause but not another? Awkward coverage problems may arise - of evidence and liability.
- Underwriters may restrict cover where losses are *exclusively* attributable to CC, but is this ever going to arise?
- One recent noted example of a “CC exclusion clause”: “*direct risks resulting from the physical impact of CC as experienced by the whole business value chain*”. (Often easier to know what you mean than to say it!)
- The law (and contract drafting) is likely to have to develop to accommodate such issues posed by “CC losses”.

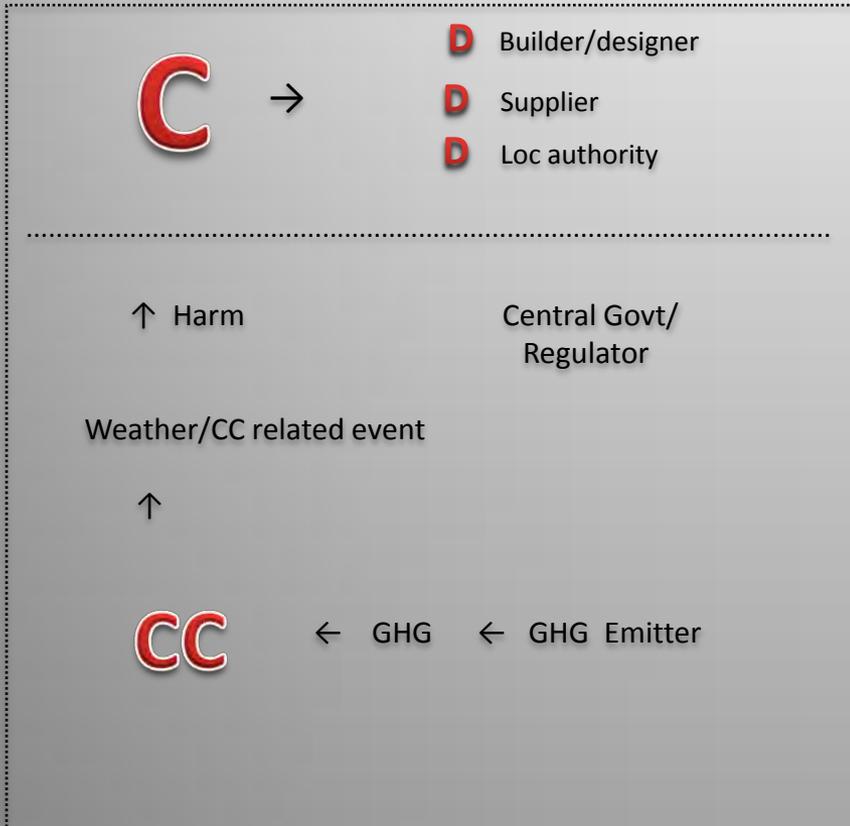
6. Liability Issues

REGIME OPTION	EFFECT/FEATURES
Mandatory insurance	Would help afford protection to 3 rd parties against loss but assumes risks may be insurable. Likely only if govts obliged to meet gap for v high risk activities which private market may not insure.
Prohibition of insurance	Most unlikely course for encouraging loss prevention. Might expose governments themselves to claims. Some examples (eg Netherlands, flood compensation).
Strict liability	Adopted in certain territories/spheres already (water, pollution) which <i>might</i> afford protection for some CC-related losses. Encourage precautionary behaviour, but may stifle innovation.
Fault-based liability	In operation for most liability classes in most established jurisdictions - seen as tool for measured transition, but pressure on boundaries/clarification.
No liability	Most unlikely as would require legislation, create major hardships/inequalities and expose governments to potential compensation claims.
Limited liability	Given scale of losses in issue private market/capital providers may be/feel obliged to limit their own exposures and <i>may</i> be mirrored by legislation.

6. Liability issues

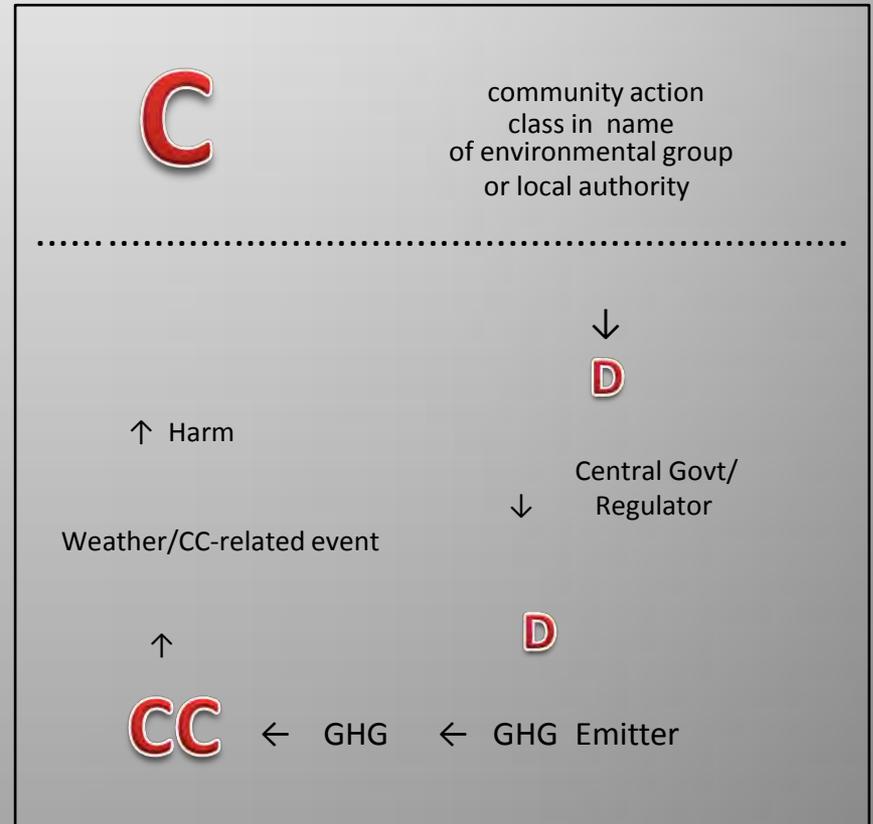
Liability claim v related party

Claim for damages for breach of contract or in tort
(negligence or nuisance)



Liability claim v unrelated party

Claim often for injunction to abate public nuisance or for breach of statutory duties rather than damages but attempts to seek to claim compensation and/or extend boundaries of tort law



6. Liability issues

based on existing English law principles/UK experience

FAULT LIABILITY TRIGGER	RELATED PARTIES	UNRELATED PARTIES
Cause	Loss from weather/CC-related event + dfndt's failure to factor in condtns/regns in its service to C caused loss	Loss from weather/CC-related event caused by CC from Co's GHG emissions or Govt reg'n more generally
Contribution	Contributing causes (and own contributing liability) not bars to liability being estabshd. Apportionment and jt + sev lbly precedents have been estblshd in similar contexts.	Even if causal link made on bal of probs, no. of potential contributors /contributory causes fuels sceptics' doubts that such actions may succeed. Ct resistance to applying jt + sev princs in asbestos cases where no rel'nship. Apportionment of so many between so many may produce v small recoveries.
Date of knowledge/ foreseeability	Matter of contention : at what date shd consider whether any harm envisaged or knowledge assesd for steps to have been taken to avoid/mitigate loss? Still to be tested. IPCC landmark dates of 1990, 1995 and 2007 have all been suggested. Scientific evidence will help settle feasibility /nature/cost of services t reasonably to be expected after major weather event.	Same as for related parties
Legislation/public policy	Regns are increasingly taking a/c of CC in many areas (eg bldg regns). Arguments likely over best practice/observance of min current regns. What if compliance alone known to be inadequate ? Different stdds rqrd in diff territories ? Some stat'y duties may invlve exmptns from lbly for some pub entities.	Govts may well legislate against claims of this kind being pursued. Cts may decline to try if deemed for govt to decide. UK has primarily emphasised legislative structures for emissions targeting and monitoring and anticipating impact. Confining action to fines and penalties for exceeding limits . At odds with complying emissions being actionable?

6. Liability issues

based on existing English law principles /UK experience

FAULT LIABILITY TRIGGER	RELATED PARTIES	UNRELATED PARTIES
<p>Duty Of Care (*cases alternatively brought in <i>public nuisance</i> commonly seek abatement only but <u>may</u> afford a right to damages for personal injury where unlawful acts endangered life, health etc - <u>Corby Group Litigation</u> (2009))</p>	<p>In tort, need for a duty of care to be owed by D to C, a breach of which caused C's loss. Tort law evolves to decide exactly where /when such a duty owed. Often owed if a statutory duty, but not always even where direct relations.</p>	<p>Need to establish duty of care between specific parties must seriously reduce prospects for any general actions against emitters being brought, especially given difficulties (in UK at least) of bringing mass tort actions*.</p>
<p>Breach of Contract</p>	<p>Only necessary to prove breach of contractual term, loss and link. Q of what knowlde of CC etc the D shd have had and actions taken at time of breach. Higher levels expected by professls/employers.</p>	<p>No basis for any contractual connection exists.</p>
<p>Physical Damage/ Financial Loss</p>	<p>Phys dam usually necessary if fin loss also to be recovered, save where special relations exist. Contract may limit terms/extent of such recoveries.</p>	<p>Much of "CC damage" is still yet to occur. Reduced values for coastal properties /other purely econ losses etc are often anticipatory of damage. Need for phys dam to be proved (save in ltd circs) is obstacle to recovery by claimants in such actions , also faced with other quantification/causation issues.</p>
<p>Territory</p>	<p>Forum shopping /jrsdctnl disputes v likely by nature of claims and if diff approaches adopted/conflicting decisions reached.</p>	<p>Same issues apply as for where related parties and may be more marked if some jrsdctns only entertain such actions as these.</p>
<p>Date of Occurrence</p>	<p>Nature/date/number of occurrences – bound to be highly important/contentious area for insurers (see asbestos, pollution , tobacco etc.)</p>	<p>Issues particularly arising include whether any single occurrence even identified/identifiable in allegations made. Will each GHG emission or decision to emit or other basis be deemed the trigger?</p>

6. Liability Issues - Litigation experience to date (1)

- Majority of actions already brought (in countries as diverse as US, Germany, Nigeria, Argentina, Australia) have tended to involve *no* close relationship between claimant and defendant: pressure groups or local states/communities bringing actions against investors, major GHG emitters and/or regulatory bodies.
- Purpose to bring attention to or seek information about decisions or alleged failings/omissions on the part of:
 - Financial backers, Export-Import Bank and Overseas Private Investment Corporation : aimed at obliging them to conduct environmental impact assessments on energy projects they proposed to support
 - *Friends of the Earth v Watson*
 - US Environmental Protection Agency : pursued by a number of US states and environmental groups to take regulatory action under the Clean Air Act to reduce GHGs from motor vehicles in which US Supreme Ct ruled that CO2 was a pollutant and that the EPA was required to take such action
 - *Massachusetts v EPA*
- Latest series of four cases which have progressed through the US courts now face appeals to be heard by the US Supreme Ct in the coming few months.

6. Liability Issues - Litigation experience to date (2)

Recent/pending US litigation:

- *State of Connecticut et al v American Electric Power Inc (2005,2009)*
 - *Native Village of Kivalina et al v Exxon Mobil Corp et al (2009)*
 - *Comer v Murphy Oil USA et al (2009)*
 - *State of California v General Motors Corp et al (2007)*
and *Steadfast Ins Co v AES Corp (2008)* (concerning coverage issues arising out of the Kavalina case)
- Fluctuating passage through various US courts. Fate of climate change litigation now rests in hands of US Supreme Ct.
 - Since late 2010 appeals pending in *Connecticut*, *Kivalina* and *Comer* cases. One threshold question : are cases justiciable or do they raise issues which only the legislative or executive) should decide?
 - If to be heard – further obstacles for claimants will be tested potentially at the expense of insurers . Should they not, many challenges in courts to much federal government legislation and other regulatory/climate mitigating programmes are still anticipated.
 - Other issues potentially still to be fully tested: i) standing (do state and other claimants have the necessary standing to bring actions – do actions involve “fairly traceable” injuries which are redressable)? ; ii) whether federal law pre-empts their claims; iii) whether claims involve *incurred* injury in fact .
 - *Steadfast* case concerns coverage question of whether American Electric’s insurers owed a duty to defend them in connection with the *Kivalina* claims (upon their CGL policy). Judge found in favour of insurers because no “occurrence” causing property damage had been alleged (rather than on other grounds that loss was a loss in progress or excluded by pollution exclusion). Now, too, subject of a pending appeal by policyholder.

6. Liability Issues - Litigation experience to date (3)

Wider implications:

- US cases: further illustrate many issues of critical importance to insurers going to heart of debate about whether governments (by legislation) or courts (by liability rulings) should set limits /sanctions upon acceptable GHG emissions.
- Many national govts slow to legislate domestically. Prefer to engage in international political process.
- UK : much of legislative activity in devising legislative structures, targets and monitoring. Designed to reduce future effects of Climate Change and provide for its impact.
- US: federal govt has in past been resistant to recognising many issues. Subsidiary legislatures much more active. Obama administration promoted Clean Air Act and supported argument that tort actions not justiciable. Plans for Climate Bill delayed.
- Most govts quite directly involved in/dependent upon business of fossil fuels. Source of tax revenue, producer of nuclear energy, vital support in any orderly transition to more sustainable environment.
- Especially if courts show inclination to hear cases, legislation may yet be passed to deny many potential claims. Particularly for past activities where emission of GHGs not been prohibited and even tacitly/more positively endorsed.
- Otherwise, other obstacles may be thought enough to frustrate potential claimants, but not necessarily sparing insurers being drawn into lengthy and potentially costly disputes meanwhile.

6. Liability Issues - Litigation experience to date (4)

Insurance implications:

- Much to learn from the issues stirred by the US litigation - not just for US business
- Among most pertinent early questions arising for insurers in these or similar cases are:
 - Which policies are triggered by any given claim? If claims made? If occurrence-based?
 - Do global warming claims seek to impose damages for property damage or for personal injury?
 - Are alleged damages actually caused by global warming/GHG emissions (“climate change”) fortuitous?
 - Will pollution exclusions operate to bar coverage for such claims?
 - Which categories of potential defendants need to be most concerned? In turn, which insurers and how if at all may they best safeguard their respective exposures in light of these and other rulings/legislative moves?

7. New products, new liabilities, new challenges

- **“New” products**

Three distinct categories of “new” product:

- i) **“green” policies** : not covering new types of loss linked to CC, but promote reduction of GHG emissions (many examples worldwide in respect of buildings, motor etc)
- ii) **“adapted”** traditional lines (property and liability) policies: designed to take account of CC liabilities
- iii) **“new” policies** : catering for range of activities involved with alternative energy sources, where cover less novel than the subject-matter (e.g. Wind farms). Include many linked specifically to new carbon market and “cap and trade” system, and offering carbon offsetting . Also, more specific covers still being developed (and upon which activities likely heavily to depend, with possible Govt level support/underwriting of last resort) in areas such as Carbon Capture & Sequestration (CCS). Microinsurance represents another distinct form of new product.

Each requires separate consideration and contractual provision in light of developing legislation, regulation and liability issues.

- **Reinsurance and ART products**

Over and above more traditional and important role played by reinsurance in catastrophe risk coverage a variety of alternative risk transfer products have emerged : e.g. weather derivatives (put options, caps and swaps) and catastrophe bonds.

One of most important issues to be addressed in many jurisdictions is the legal and regulatory characterisation of such transfers . Will they be governed by insurance laws ? How effectively may indemnification principles operate if some features of traditional insurance and reinsurance products are disputed in connection with CC-related risks ?

8. The Forecast?

- The English used to be noted for making conversation about the weather.
- It was seen as safe. Any shortcomings about it were beyond reproach. If they tended to be rather predictable, their weather was not.
- Discussion of it involved no express or implied criticism of anyone. No-one could be blamed for it. Not even the meteorologists, who still solemnly preach on TV what *might* be expected the next day, but subtle changes have occurred.
- “Our” weather remains relatively moderate, but this winter mainland temperatures of minus 20 degrees Celsius and “Arctic wind chill factors” have come accompanied by fuller explanations of from *where* the weather has come.
- Radar maps, from which they used simply to forecast, now shown to describe their difficulties of prediction. “Long-range” forecasts have officially been withdrawn as lacking sufficiently sound foundation. (Are they receiving legal advice?!)
- Ministers for Transport and airport chiefs stood this winter in sub-zero temperatures apologising to the media for widespread disruption. The Northern Irish Minister for Water recently resigned in apparent disgrace after many in the province went without water for days.
- Many profess to struggle with the paradox of why “UK Big Chill = Global Warming”. Similar experiences are described in countries around the globe. Others note the paradox that in the short-term the less productive the economy, if saddled with ecological and legislative constraints, the less capital is available to invest in ecologically sound longer-term strategies. Additionally, the unfairness in the eyes of others lies in changing the rules on emissions when some countries are dependent upon traditional power sources to fuel their fast-growing economies.

8. The Forecast?

- The headline story in one of the UK's recent broadsheet editions read: "***Perfect storm of climate and oil puts world into "danger territory"***", but what message is delivered if those heading for work are more pre-occupied by bleak economic or job prospects and a New Year rise in tax rates.
- The main article continued: according to the UN, "***Food riots, geopolitical tensions, global inflation and increasing hunger ... are the likely effects of a new surge in world food prices...***", brought about by the following "causes":
 - **AUSTRALIA:** Droughts and floods hitting sugar and wheat supplies
 - **US:** One quarter of all grain crops grown are now used for biofuel rather than food
 - **RUSSIA/UKRAINE:** Worst drought in 50 years saw wheat export ban in August 2010
 - **EL NINO:** Blamed for extreme weather events disrupting crop production worldwide
 - **BRAZIL, INDIA, INDONESIA, CHINA, RUSSIA:** Swelling (sic) middle-classes are switching to meat-based diets putting pressure on grain stocks needed to feed livestock.
- Spare some pity for the court or the lawyer in any jurisdiction expected to predict with any certainty how principles of causation, as well as many of these other issues highlighted, will ultimately be applied to the swirling 2011 and onwards world of mutual obligations and duties owed. So, too, the underwriter or contract draftsman expected to anticipate the unfolding of all these perils.
- One does need to keep monitoring the radar, however, or it really will be just left to guesswork – or tea leaves!

Acknowledgments

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Too many other additional sources and materials have been drawn upon to acknowledge or cite here, but of particular assistance in respect of certain aspects of this presentation have been: *The Finance of Climate Change, A Guide for Investments, Corporations and Investors*, Ed. Kenny Tang, 2005, *Risk books; Coping with Climate Change - risks and opportunities*, *Climate Change Research Report, 2009*, Dr Andrew Dlugolecki & Ors, CII; *Insurance Coverage for Global Warming Liability Claims*, James Malloy and John M Sylvester, K&L Gates LLP, *Tort Trial & Insurance Law Journal*, Spring/Summer 2010.

For those interested in participating in or being kept informed about future events and activities of the AIDA Climate Change Working Party please contact me at: t_hardy@btconnect.com; T: +44 20 7722 6981; F: +44 20 7586 5736. The first Working Party meeting is scheduled to take place on **26 May 2011** at the AIDA Europe Conference in Amsterdam, details of which may be found at:

<http://www.aida.org.uk/AIDAEurop/Forthcoming-events.asp>

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