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Environmental Insurance: A Business Lawyer's Guide

Contamination legal liability policies represent an important hedging option for environmental contamination risk that business lawyers should consider for their clients that face appropriate fact-specific environmental risk situations. The author provides a roadmap for potential uses of these new environmental insurance policies, highlights legal pitfalls for unwary clients, and identifies the areas that lawyers should address in negotiations leading to the purchase of these insurance products.

by **Arthur J. Harrington**

The insurance industry is creating new products that allow policyholders to shift financial responsibility for environmental liabilities in exchange for payment of premiums. Numerous factors have led to the development of these environmental insurance policies, including the accounting profession's recent adoption of a new standard known as FIN 47. This is a new interpretation of financial accounting standard 143 (accounting for asset-retirement obligations). FIN47 is an accounting guidance that requires inclusion of environmental liabilities in financial statements when a business decides to close a manufacturing facility. Lawyers need to be well-versed in this emerging insurance area, because this trend provides opportunities for the savvy business client and potential pitfalls for the unwary client.

This article provides a roadmap for potential uses of these new environmental insurance policies, highlights the important legal pitfalls for the unwary business client, and identifies the areas that business lawyers should address in negotiations leading to the purchase of these insurance products.



Factors Promoting Environmental Insurance Solutions

Several factors have given rise to insurance-based solutions after a less than satisfactory experience of parties involved in transactions involving contaminated property. Federal and state mandates to reduce agency budgets have resulted in staff cuts at the federal and state agencies responsible for implementing the command/control structure for overseeing the remediation on contaminated property. Due to these staff cuts parties are unable to obtain timely written evaluations and assurances from these agencies on the nature and extent of contamination that may exist on a property. Given the concerns about strict-liability statutes for ownership of contaminated property,¹ buyers of such property face time-consuming and expensive due diligence inquiries to determine the nature and extent of contamination. Frequently, this due diligence requires the parties involved in a sale transaction to have adequately identified the nature and extent of contamination.² For example, the Wisconsin Department of Natural Resources (DNR) has authority to assist a person to determine the person's rights and responsibilities regarding environmental pollution on a property. The DNR has authority to issue assurance letters regarding the liability of that person for contamination on the property, the nature, type, and extent of environmental pollution on the property, and the adequacy of any environmental investigation conducted on the property. Such agency assurances frequently are necessary to satisfy parties that the state agencies will not require expensive remediation that can affect the parties' assessment of the liability associated with ownership of the property. The reduction of agency staff has created greater uncertainties for property buyers and sellers, because agency assurance letters are more difficult to obtain in a timely fashion to accommodate redevelopment transactions.

Another factor influencing the use of insurance solutions is the development of more risk-based remediation clean-up standards by state and federal agencies. In the earlier history of the command/control structure, state and federal agencies established clean-up standards that were associated with the highest-risk use for the



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