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September 2004

The Impact of the EU'S Newly-Adopted "Polluter Pays" Environmental Legislation: Learning from the U.S. Experience

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Overview

On April 21, 2004, the EU Council of Ministers definitively adopted the directive of the European Parliament and of the Council on environmental liability with regard to the prevention and remedying of environmental damage. The new directive 2004/35/CE has now been published in the *Official Journal of the European Union* (the "Environmental Liability Directive"). The directive must be integrated into the national law of the 25 Member States of the European Union by April 30, 2007.

Although the EU Member States have a period of three years to implement the Environmental Liability Directive by enacting national rules and regulations, companies should start to consider the new exposure issues associated with environmental liability for operations within the European Union and the best way to deal with them. The issue goes beyond those industrial companies doing business in the EU. Indeed, various international operators in certain service industries (such as insurance services) will be indirectly affected by this new legislation in the coming years.

Companies doing business in the United States will recognize the impact of the U.S. experience with Superfund and similar statutes on the new EU Directive. Thus, some international operators may look to the U.S. experience for guidance with regard to the new EU legislation. This issue is further discussed below.

The Environmental Liability Directive implements the *"polluter pays"* principle within the European Union. It represents some 15 years of effort by the European Commission to bring harmonized rules on environmental liability to the EU. The new directive implements principles set out in a European Commission white paper, published in February 2000 for public consultation, on the various policy options with regard to environmental liability. Following the public consultation, the proposal for the new directive was issued by the Commission in June 2002. As part of the EU's co-decision procedure, the Council of Ministers and European Parliament reached agreement regarding the conciliation procedure on February 20, 2004. This was followed by formal approval of the two institutions in March and April 2004. With so much at stake, the issue of environmental liability gave rise to considerable lobbying by business interests in Brussels during the period 2000-2004.

Terms of the Directive

Scope of Liability

The Environmental Liability Directive covers environmental damage to (i) land, (ii) water and (iii) biodiversity. Only "measurable" damage falls within the scope of the directive. For certain high-risk occupational activities listed in an annex, all environmental damage is covered and strict liability applies. Thus, *an operator may be held liable even where it is not at fault or has not committed an act of negligence.* These activities include, amongst others, industrial and agricultural activities requiring permits under the EU's 1996 Integrated Pollution Prevention and Control Directive, waste management operations, the release of pollutants into water or air, the production, storage, use and release of dangerous chemicals, and the transport, use and release of genetically modified organisms. For other occupational activities, only damage to protected species and habitats is covered, and liability is incurred only based on the fault or negligence of the operator.

There is no ceiling on the amount that polluters may be required to pay to remedy environmental damage.

In certain cases polluters are exempt from liability. Moreover, the Environmental Liability Directive allows potential polluters to rely on reasonable defenses. For example, environmental damage caused by *force majeure* (such as storms and armed conflicts) will not give rise to liability. Other defenses are potentially available to operators, but their use is subject to several conditions. For instance, Member States may decide to exempt operators which have caused environmental damage if those operators are able to demonstrate that the damage was caused by activities or emissions expressly authorized by public authorities and if they can also prove that they were not at fault or negligent.

Member States may also decide to exempt from liability operators who demonstrate that their activities or emissions were not considered likely to cause environmental damage according to the state of scientific and technical knowledge at the time when the emissions were released or the activity took place.

Remediating Damage

The Environmental Liability Directive sets out different remedial measures depending on the type of damage.

In terms of biodiversity damage and water pollution, remediating environmental damage will be achieved, as a general rule, through the return of damaged habitats, species, natural resources and/or waters to baseline condition and compensation for any interim losses incurred. Remediating polluted soil involves decontamination until it no longer poses a significant risk to human health. Restoration is done through rehabilitating, replacing or acquiring equivalent damaged natural resources and/or services at the original damage site or at a different location. Indeed, where a damaged site itself cannot be restored, either another site which is of equivalent environmental value nearby or another site which fulfills the same environmental role must be environmentally improved.

Once Member State authorities have developed a reasonable range of restorative options, they may evaluate the proposed options according to established minimum standards criteria: (i) the effect of each option on public health and safety; (ii) the cost to carry out the option; (iii) the likelihood of success of each option; (iv) the extent to which each option will prevent future damage and avoid collateral damage as a result of implementing the option; and (v) the extent to which each option benefits each component of the natural resource and/or service.

Temporal Application

Member States have until April 30, 2007 to integrate the terms of the Environmental Liability Directive into national legislation. The directive will not apply retroactively. *Thus, operators will not be held responsible for damage resulting from activity before the entry into force of the implementing legislation.* In particular, the directive will not apply to damage caused by waste where disposal took place lawfully in authorized disposal facilities before the directive is applicable in the EU Member States. Once the terms of the directive go into effect, it may be expected that, in many cases, the issue of the exact temporal nature of environmental damage will give rise to disputes, particularly with regard to business activity pursued on a continuous basis before and after the enforcement date.

The Environmental Liability Directive also sets out a means for alert operators to establish a temporal defense with regard to past environmental damage. *Within one year of the enforcement date of the terms of the Directive in the EU Member States, operators may submit to national administrative authorities a statement identifying any environmental damage that may have been caused by their activities before the date the directive became applicable.* Industrial operators may want to carry out a detailed environmental audit in order to make a clean break with the past. However, the advantage of such a temporal defense should be weighed carefully in connection with any obligations for past pollution which could derive from current rules and regulations.

Learning from the U.S. Experience

A New Market for Environmental Insurance

The Environmental Liability Directive does not set out any environmental insurance requirements. However, it can be expected that *a whole new market in environmental insurance products, adapted to the terms of the directive, will begin to emerge* (although unlimited potential liability may pose a problem from an insurance point of view).

It may be anticipated that there will be some public intervention on the insurance issue, to the extent that Member States have the obligation to encourage the development of environmental insurance products adapted to the terms of the directive. Moreover, by 2013 (six years after the implementation deadline), the European Commission must file a report on the insurance issue, in particular with regard to any possible mandatory insurance requirements (and the scope thereof) and the potential introduction of a ceiling on liability.

If the American experience is any guide, it can be expected that an active market for environmental insurance, with a number of different products,

will develop to meet the environmental insurance needs of companies operating in Europe. The fact that Member States have various options with respect to the scope of liability may complicate this process. However, a countervailing consideration is that past contamination will not necessarily be required to be cleaned up, a fact that will greatly simplify the underwriting process and make insurance more affordable. By the same token, since insurance companies will not want to be responsible for prior contamination (since their product will not be priced to cover it), they may be particularly insistent on the conduct of baseline due diligence before agreeing to insure a given property.

Avoiding Superfund Pitfalls

The drafters of the new directive have clearly drawn several important lessons from the U.S. experience with Superfund and similar statutes. Superfund's retroactive, strict and joint-and-several liability scheme has spurred significant cleanup in the U.S., but it has come at a great cost in terms of ease of transferring properties, litigation risk and expense, and, in the eyes of some people, unfairness to companies whose disposal practices complied with all laws at the time the disposal took place. Several of the exemptions allowed by the Environmental Liability Directive represent efforts to remedy those problems.

However, these limitations also represent potential obstacles to achieving the cleanup goals of this new initiative. Most of the cleanups under Superfund have been precisely those where the disposal was legal at the time it occurred, and many companies would have been able to argue successfully that they were not negligent or that their activities complied with the "state of the art" at the time. However, those sites still need to be cleaned up, and the U.S. Congress decided that it was more equitable to put the financial burden on the companies that created the pollution (even if non-negligently) than on the general public. *It remains to be seen whether the less Draconian scheme envisioned by the Environmental Liability Directive will be effective in achieving cleanups.* One of the hidden successes of the Superfund law is the extent to which it has "privatized" cleanups. That is, cleanup activity in the U.S. is not solely dependent on government enforcement but, instead, often flows from private companies insisting on cleanups in the context of business transactions because they do not want to inherit other companies' liabilities. The U.S. cleanup scheme has also been supported by the availability of private rights of action, and many cleanups have occurred because of lawsuits brought by private parties rather than the government. It is likely that the lack of a private right of action under the Environmental Liability Directive will mean that it will be less successful in stimulating cleanup activity than Superfund has in the United States.

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