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CLIMATE CHANGE LAW. CURRENT PERSPECTIVES.

Climate Change and Insurance Law

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As the effects of climate change escalate, both in terms of physical consequences and regulatory responses, there has been a proliferation in in research and review of the likely issues which the finance and insurance industries will face.

A number of regulatory bodies have recently grappled with these nascent legal issues. For instance, the IAIS (International Association of Insurance Supervisors) issued a comprehensive statement in advance of the COP26 Conference detailing a proper approach to the issue of climate change and promising to advance its work to address risks and opportunities involved: https://www.iaisweb.org/uploads/2022/01/210525-Application-Paper-on-the-Supervision-of-Climate-related-Risks-in-the-Insurance-Sector.pdf.

This followed a general 'Supervisory Statement' from the Prudential Regulation Authority ("PRA") in 2019 regarding climate change relevant to all UK insurance and reinsurance firms and groups: https://www.bankofengland.co.uk/prudential-regulation/publication/2019/enhancing-banks-and-insurers-approaches-to-managing-the-financial-risks-from-climate-change-ss. This set out a review of the then current practices in the banking and insurance sectors, the risk factors from which financial risks from climate change arise (specifically physical risks and transition risks, further detailed below) and the PRA's expectations as to by whom those risks were to be managed going forward from governance, financial risk management, strategy setting and disclosure perspectives.

Very recently, on 24 May 2022, the Bank of England published its 2021 Climate Biennial Exploratory Scenario which explored the financial risks posed by climate change for the largest UK bank and insurers: https://www.bankofengland.co.uk/stress-testing/2022/results-of-the-2021-climate-biennial-exploratory-scenario#:~:text=The%20Climate%20Biennial%20Exploratory%20Scenario%20(CBES)%20includes%20three%20scenarios%20exploring,Action'%20(LA)%20scenario.

There are broadly three novel or enhanced risks to which insurers are exposed in this context.

1. First, there is the increased risk of loss, which includes the obvious physical risks associated with climate change, for instance changing weather patterns, more extreme weather, and rising sea levels. This would impact a variety of policies, most obviously property and casualty insurance.

2. Secondly, there are the risks associated with transition. These risks arise from the strategies required to move towards a low-carbon or net zero economy, such as new climate change-driven regulations or policies, novel technologies or changes in carbon prices.

3. Finally, there are specific liability risks involving a wide variety of policies, for example CGL, professional indemnity and D&O.

Against this backdrop, the remainder of this blog post addresses some of the potential legal issues which may arise in respect of climate change litigation and arbitration in the insurance sector.

'Occurrence'

Many liability policies have an 'occurrence' element as part of the two-stage trigger for coverage. One question is whether or not a particular climate-change-based event would come within the definition of an 'occurrence.' It is generally defined in the policy and often along the lines of an 'accident, including continuous or repeated exposure to conditions' which causes 'bodily injury' or 'property damage'. It also sometimes includes a stipulation that the injury or damage is neither expected nor intended by the insured. In typical occurrence-based policies, the injury or damage must take place within the policy period for coverage to be triggered.

In contrast, in respect of non-product liability claims, Article III.V(1)(a) of the Bermuda Form provides for the event itself to take place within the policy period:

'...there is an event or continuous, intermittent or repeated exposure to conditions which event or conditions commence on or subsequent to the Inception Date, or the Retroactive Coverage Date, if applicable, and before the Termination of Coverage... which cause actual or alleged Personal Injury...[or] Property Damage...'

Article III.V(2) expands the definition further, including aggregation, and provides that injury or damage which is expected or intended by the insured is not included as an 'occurrence.'

A preliminary question is whether some climate change 'occurrences' can actually be called 'accidents' or were 'expected or 'intended' in circumstances where, for instance, energy companies are well aware of the emissions released into the atmosphere and their effect: *AES Corp. v. Steadfast Ins. Co.*, No. 100764, 2011 Va. LEXIS 185 (Va. Sept. 16, 2011). In those circumstances, unless there is coverage for known occurrences, such claims would fall outside the policy.

Putting that to one side, the difference in temporal scope between these two different occurrence-based definitions noted above also may present very different outcomes in a climate change case. In standard CGL policies, the damage must occur in the policy period; this could be very difficult to pinpoint. For Bermuda Form cases (at least for a 'type I' occurrence which is the definition set out above), it is the timing of the event itself which is crucial.

An interesting example of where this may matter is the emissions cases, where claims are brought for the adverse effects of the release of greenhouse gases into the atmosphere, such as in the recent case of *Smith v Fonterra* [2021] ZCA 552. There, the Court of Appeal of New Zealand considered a claim brought by an individual that the release of greenhouse gases by seven dairy companies were breaches of the torts of nuisance, negligence and a novel duty of care. In principle, under a standard CGL policy, the 'event' (namely, the emission) may have occurred long before the policy incepted, and yet the damage would likely not manifest until much later during the policy period. On the other hand, where there are emissions regulations in place (as is more likely now), damage caused by a company exceeding those levels may trigger coverage under a Bermuda Form policy even if the damage is not felt until much later in the future.

And what of continuing emissions or greenwashing? If a policy contains a limitation of a maximum sum for losses arising out of 'any one event,' does every emission, or every provision of misleading information, count as one event or occurrence? Similar questions arise where the policy contains an aggregation clause and 'Integrated Occurrences' under the Bermuda Form. English courts have traditionally emphasised that the answer to these questions is context and policy language-specific, see *Lloyds TSB v Lloyds Bank Group Insurance Co Ltd* [2001] 1 Lloyd's Rep IR 237 at p.241. But aggregation of claims in respect of emissions and false disclosure may be easier to make out under certain types of aggregation clause, particularly in light of the Supreme Court's indication in *AIG Europe Ltd v Woodman* [2017] UKSC 18 that, based on the language in that case, there had to have some 'inter-connection between the matters or transactions' for them to be aggregated.

Pollution Exclusions

Many policies now contain a pollution exclusion clause,

and although the clauses differ, they are often broadly worded. They typically provide that there is no cover for 'bodily injury' or 'property damage' that 'would not have occurred but for the actual or alleged, discharge, dispersal, seepage, migration, release, or escape of pollutants'. The precise definition of 'pollutant' varies but is often defined as including 'any solid, liquid, gaseous or thermal irritant or contaminant, including smoke, chemicals, and waste' (together the 'Pollution Exclusion').

Could this apply to cases involving the effects of climate change? This will in part depend on the exact type of case. For instance, if a rise in temperature caused the seal on a container to warp so that its contaminant contents escaped, or an extreme storm knocked it over which broke the seal, one can see this as comfortably being caught within the Pollution Exclusion – but that is because such a scenario is not really a direct case about the effects of climate change at all. Of course, insurers should be mindful that this type of case might increase with more extreme weather conditions and so their individual pollution exclusion is worth reviewing.

But what about air pollutants, for instance nitrogen oxide, sulphur dioxide, hydrocarbons, carbon monoxide and carbon dioxide, all being pumped into the atmosphere from particular coal stations or transport which, it is alleged, have caused or contributed to the increase in asthma attacks in city-dwellers? One would expect to have to leap over a number of hurdles to show causation in this example, but there is an argument for air pollutants, such as carbon monoxide, nitrogen oxides and hydrocarbons, being caught within the Pollution Exclusion.

As for carbon dioxide, the position is perhaps less clear: it is present in clean air and we ourselves produce it, albeit the percentage in clean air amounts to approximately 0.04%. There is some research which has suggested that an increase in carbon dioxide levels has caused an increased pollen counts due to rising temperatures and that in turn has worsened asthma: https://ec.europa.eu/environment/integration/research/newsalert/pdf/292na5_en.pdf. If sufficient causation could be shown, then would carbon dioxide be characterised as a 'pollutant' and therefore caught within the exclusion? Given its inherent presence in the atmosphere and the indirect way it may cause injury or damage, the case is rather less persuasive than for other air emissions but not necessarily fatal. However, given the increasing global regulation on the level of emissions, it could be that surpassing the permitted emissions level would suffice.

The Bermuda Form Pollution Exclusion, Article IV.K, provides for what is *prima facie* an absolute pollution exclusion, albeit with three 'escape' clauses which 'write back' cover in certain circumstances. The first part of the exclusion is of note in that it could be interpreted to include the effects of climate change:

'1(a) liability for Personal Injury, Property Damage or Advertising Liability arising out of the Discharge of Pollutants into or upon land or real estate, the atmosphere, or any watercourse of body of water whether above or below ground or otherwise into the environment; or

(b) liability, loss, cost or expense of any Insured or others arising out of any direction or request, whether governmental or otherwise, that any Insured or others test for, monitor, clean up, remove, contain, treat, detoxify or neutralize Pollutants.

This Exclusion K applies whether or not such discharge of Pollutants

(i) results from the Insured's activities or the activities or any other person or entity;

(ii) is sudden, gradual, accidental, unexpected or unintended; or

(iii) arises out of or relates to industrial operations or the Waste or by-products thereof.' (emphasis added)

This has considerable scope. *'Pollutants'* are defined in Article III.Y of Form XL-004 as *'any solid, liquid, gaseous or thermal irritant, contaminant or toxic or hazardous substance or any substance which may, does or is alleged to affect adversely the environment, property, persons or animals, including smoke, vapor, soot, fumes, acids, alkalis, chemicals and Waste.'* On that definition alone, gaseous emissions into the atmosphere such as those discussed above appear to fit, and they are discharged into the atmosphere as per 1(a). Providing that causation can be proved, this exclusion may well bite.

However, one must take into account the purpose behind

the clause. In *Colony Insurance Company v Buckeye Fire Equipment Co.* No. 3:2019cv00534 Document 26 (WDNC 2020) the US District Court for the Western District of North Carolina reminded the parties that the purpose or intention of the clause was important in its construction in that it seeks to protect against the *'prototypical environment harms,'* i.e. those which are dispersed (escape, released etc) into the environment. This also forms the backbone of the Ontario Superior Court of Justice's reasoning in *John Hemlow v Co-Operators General insurance Company* 2021 ONSC 664 when deciding the ambit of an ambiguous clause entitled 'Total Pollution Exclusion'.

The release of gaseous emissions into the atmosphere is clearly a release into the environment and so satisfies that requirement, but the overarching principle that the claim must come within the purpose or intention of the Pollution Exclusion is worth considering in the context of rising temperatures as a result of greenhouse gases. Is this sufficiently direct to come within the purpose of the Pollution Exclusion? It has a different flavour to the typical scenario of neon green goo escaping barrels labelled 'HAZARD' into a stream which then contaminates water supplies. This is particularly true when one considers that humans have been pumping greenhouse gases into the environment for centuries, and it is only the recent accumulation of those gases, and knowledge of their effects,which is causing the global issue. Green goo dripping into a stream has always been 'A Bad Thing'; pumping carbon dioxide into the atmosphere has not (and, notwithstanding the difficulties, is still broadly permitted for the sake of economic growth). Whilst not strictly relevant to the interpretation of the Pollution Exclusion, the fact that there is separate 'Environmental Liability Insurance' available makes the case for this type of climate change harm falling within it is even less compelling.

Returning to the Bermuda Form, the 'escape clauses' of its pollution exclusion clause entail (i) product liability; (ii) intentional discharge performed for the purpose of avoiding or mitigation injury or damage which would otherwise be covered; and (iii) a 'time element' exception providing cover where the discharge is not expected (or intended) and the insured becomes aware of the discharge within 7 days (or other endorsed time period, for instance 20 or 80 days).

A 'typical' claim for coverage in respect of damage or injury caused as a result of climate change is unlikely to fit within any of those three exceptions. The latter may be relevant in particular circumstances but it will be less common that a case would involve the unintentional discharge of gaseous air emissions of the type discussed above, of which the insured became aware quite quickly, which then caused some climate change-related injury or damage.

Climate Change Harm Exclusions?

One can expect a proliferation of climate change harm and similar exclusion clauses to materialise in a variety of different types of policies. What might these look like? Of course, the answer to this question will depend on the type of policy and risk profile in any particular case, but there are some aspects which may typically feature.

It may be that a claim concerning climate change harms can be characterised as a 'known occurrence'. The effects of burning fossil fuels and its impact on the environment has been known for a considerable length of time. Insofar as an insurance policy excludes occurrences known to the insured (or an executive officer or similar thereof) then this simple exclusion may be sufficient. So too for any 'previously notified occurrences' if the claim can be characterised as such.

This may not work in every case and more detailed climate change exclusion clauses may be required. In any event, given the likelihood of climate change products tailor-made to this emerging sphere, general liability insurers will probably increasingly utilise specific exclusions. One way of doing this is to link the exclusion to an insured's targets of reduced emissions: for example, where the policy defines the insured's strategy to reduce emissions to a particular percentage by a certain date, or requires that they use 'best endeavours' or similar to do so, then the policy will cover losses unless that they fail to reach that target: see for example https://chancerylaneproject.org/climate-clauses/exclusions-from-insurance-coverage-for-climate-harms/.

Cover for Defence Costs

Another important type of clause to consider in this context is the provision of coverage for defence costs,

particularly where it is irrelevant whether the claim brought against the insured is successful. More and more strategic claims are being brought against both state and private entities with the aim of changing corporate behaviour and as a tool to shift industry focus to climate change: https://www.lse.ac.uk/granthaminstitute/wp-content/uploads/2021/07/Global-trends-in-climate-change-litigation_2021-snapshot.pdf. There is also likely to be an increase in greenwashing cases as way of policing ESG disclosure requirements.

This might mean an increase in specific products targeted by climate-activist litigation, and further exclusions in general liability policies and – in particular for greenwashing issues – D&O insurance (as to which, see the Week 2 Blog Post here: https://essexcourt.com/climate-change-in-law-current-perspectives-week-2/). In addition, the appetite for class action-type claims is growing (see, for instance, the Dutch Shell case), not only in the United States but also across Europe. EU Directive 2020/1828 *'Representative actions for the protection of the collective interests of consumers'* was adopted in late 2020 and Member States have until December 2022 to implement it. Whilst class actions are still limited in the UK, it is likely that eventually the UK will join the bandwagon. In any event, the increasing hunger for climate change litigation is an ideal breeding ground for mass class action-type lawsuits, and defence costs coverage should reflect that risk.

And it is not just individuals or groups of individuals targeting companies. Public authorities are starting to use litigation against the private sector in respect of the rising cost of climate change. States and cities in the United States are resorting to litigation against the big fossil fuel companies over claims that they breached consumer protection laws or knew of the effects of climate change and failed to issue warnings, for example in *City of New York v Chevron, Connecticut v Exxonmobil* Civil Case No. 3:20-cv-1555 (JCH) and *Baltimore v BP Plc et al* 141 S.Ct. 1532 (2021).

As with climate change in general, this may encourage a separate or additional aspect – or price – of cover for these types of defence costs, particularly for the major fossil fuel companies.

Parametric Insurance

It is also possible that litigators may have to grapple with an increase in claims under parametric insurance policies, which hang on a measurable index and predefined trigger events without necessarily requiring damage: https://www.insdevforum.org/tripartite-project-launched-in-mexico-by-ministry-of-finance-and-public-credit-the-idf-undp-and-the-german-government-to-develop-an-insurance-programme-to-protect-climate-vulnerable-farmers/. For instance, in respect of flooding, insurers could in theory underwrite and price risks using particular models and information, so that once water reaches a particular level the insured receives a payout regardless of damage actually incurred.

So far as we are aware, there had been little or no consideration of these types of policies by the courts but this class of insurance may well become an increasingly important element of an insured's risk spread, particularly in respect of assets in respect of which it is hard to attract traditional indemnity cover or for losses independent of physical damage.

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