WHEN ENVIRONMENTAL DISASTERS STRIKE:
How to Plan For and React to Catastrophic Events In Order to Minimize Liabilities and Facilitate Insurance Recovery

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INTRODUCTION

Even a company that is in compliance with applicable environmental laws and permits, and implements measures to avoid disaster, might receive a late night call reporting that a fire, explosion, flood or other catastrophic event has occurred at the company's premises, and police officers and television crews are on the scene. Such events could cause environmental contamination and other forms of property damage and third-party liabilities, which could result in increased expenses and extended revenue losses. These events also tend to result in investigations by regulatory agencies (such as the EPA and OSHA), and lawsuits by those harmed, such as employees, neighboring individuals or businesses, and customers or suppliers whose businesses also are impacted by the loss.

The actions a company takes before and immediately after a catastrophe often affect the extent to which the property is protected, the amount that the cleanup will cost, whether lawsuits will be filed against it, and to what extent insurance coverage will be available. Careful pre-disaster planning that considers potential environmental impacts can streamline and help facilitate post-disaster actions and communications, allowing for an integrated response by the company's environmental, legal, financial, and risk management professionals.

This article discusses environmental risk management best practices, both before and after an emergency, from the environmental, insurance, and accounting perspectives. Below are steps companies can take to integrate environmental compliance and emergency response with insurance claims management and cost segregation, which should minimize liabilities and facilitate the recovery of insurance proceeds.

PRE-LOSS PLANNING

Businesses can (and should) take certain steps pre-loss that will facilitate the environmental response and the insurance claim adjustment process post-loss.

ESTABLISH A MULTI-DISCIPLINARY CRISIS MANAGEMENT TEAM

A pre-established crisis management team can assist a company in quickly and efficiently addressing the various issues that follow an environmental disaster, including damage to company property, damage to third-party property, bodily injury, and interruption of normal business operations. The team should include internal and external professionals with knowledge of the company operations and environmental compliance and of environmental emergency response protocols, such as individuals in the risk management, legal, human resources, purchasing, finance, operations, and environmental health and safety departments, as well as accounting claims consultants. This team should be led by an Environmental Response Manager ("ER Manager"). This individual can be a third party who has immediate access to additional technical resources and expertise commonly not found within.

PRE-LOSS ENVIRONMENTAL "MANAGEMENT" RATHER THAN "MITIGATION" PROMISES

While many property owners and managers are familiar with restoration and mitigation companies, and may have "Preferred Client" agreements with such companies for post-disaster response, these agreements and the services they promise often provide little benefit in the wake of a large-scale environmental disaster. The potential environmental hazards associated with a property damage claim, even in a commercial, residential or institutional building, are many and often not initially apparent. Asbestos and lead paint can be readily dislodged with a water event.[1] Contamination, including dioxins and furans from PCBs and mercury in ballasts and switches, can be dispersed widely in a small fire.[2] Legionella and excessive mold can spawn from a neglected or damaged HVAC system. In response to super storm Sandy in New York, flooding caused interior building fuel tanks to float from their saddles and burst, releasing copious amounts of oil into the contained flood waters, coating interior surfaces. These hazards are exaggerated in a hospital or medical facility and much larger in a manufacturing facility with chemical use.

While many of the standard property damage restoration and drying companies tout environmental expertise, few have proven experience in-house. Further, while many of the hazardous response firms understand liquid and chemical spills, few have drying and restoration capabilities. Specialty hazards such as blood-borne pathogens or radionuclides require very special expertise.

Contractors need to be managed. Therefore, there is a need to have multiple resources in place, under contract, and an ER Manager to properly and effectively deploy and supervise these resources. It is important that this be done from the onset to minimize the likelihood that an insurance carrier will "disallow" or deny coverage for charges they deem to be excessive after they already have been incurred.

The response to flooding resulting from super storm Sandy is a perfect example. Property owners responded to flooded basements by calling in pumping resources. This instinctive reaction often proved to be incorrect as these general contractors were pumping oil-laden water, at high concentrations, into city streets and even adjacent vacant properties! The risks and hazards became further exacerbated by the use of gas-powered generators that caused potentially deadly carbon monoxide build-up in subterranean and confined spaces.

Experiences like this demonstrate the need to have the proper resources and management in place BEFORE the loss.

The property restoration contracting industry typically offers simple "Preferred Client" agreements that guarantee the services of the restoration contractor before the contractor deploys services to others who have not signed such an agreement. The contractor commits to a response time, commonly within 8 hours. There is a general description of work to be performed, but no specifics concerning the actual site-specific scope of services. These contracts include time and materials cost and billing schedules, with multiple labor categories and dozens of listed unit prices for every possible piece of equipment or material that may be used, down to a single trash can, paper towel, or rag. The moment the contractor sets foot on the site, the response obligation is satisfied and the meter starts ticking against the unit price schedule. The rental rates for equipment start accumulating regardless of whether the equipment is appropriate, adequate, or properly deployed. Required equipment may not even be on site. When the unaware owner, in turn, submits these costs to its insurance carrier, it often will result in invoices being rejected or reduced. This then leads to, or compounds other, payment delays and disputes.

An ER Manager should apply standard construction management procedures to control the scope, budget, quality, schedule and safety of environmental emergency response actions. An emergency response action should be considered a fast-track project, and pre-disaster planning and proper contracting can prevent or minimize inefficiencies, overbilling, and payment disputes after a major loss. An ER Manager can control and save costs for the owner/insured by directly contracting and coordinating with the event-specific subcontractors (e.g., for waste disposal) in order to save on mark-ups and avoid start-up delays. A portion of these tasks should be able to be procured in a lump-sum fashion, setting the costs in advance. The ER Manager should be independent of the response contractors and aligned with the owner. As such, the ER Manager will evaluate the geographic coverage, technical disciplines, and limitations of potential response contractors.

As part of a company's disaster response planning team, the ER Manager should review, assemble and protect all information pre-loss that may be needed

[1] E.g., high-rise sprinkler head breaks overnight on 30th floor of a metropolitan high-rise building sprayed with asbestos fireproofing, resulting in extensive surface and street asbestos contamination, including municipal storm drains.

[2] E.g., small fire in the 5th floor copy room (copier overheating) resulting in PCB ballasts burning and contaminated smoke confirmation on upper 15 floors.

in order to respond to environmental impacts after a loss, such as floor plans, fire response plans, locations of utilities, AST/UST locations, operations and management plans, environmental compliance permits, hazardous materials storage (MSDS), and use data. Pre-loss, the ER Manager also should establish regulatory reporting and notification procedures as well as a written emergency assessment and response protocol.

PRE-LOSS INSURANCE AND ACCOUNTING PLANNING MAKES GOOD BUSINESS SENSE

There are several pre-loss steps that companies can take to help facilitate the insurance claim adjustment process. For instance, every year companies should carefully review their insurance policies to make sure that they provide sufficient coverage for the various environmental (and other) risks that they face. While companies should review their entire policies, special attention should be paid to the scope of coverage provided (i.e., coverage grants and exclusions); the amount of coverage available for different types of losses (i.e., limits and sublimits, as well as retentions/deductibles); and dispute resolution provisions (e.g., ADR clauses, choice-of-law clauses, choice-of-forum clauses, and contractual limitations periods).

Companies also should develop and implement an accounting structure that provides for the segregation of costs associated with the disaster from costs associated with normal operations. The guidelines should include cost-charging instructions for procurement activities and labor charging for, among other things: (1) normal payroll; (2) damage assessment; (3) clean-up labor; (4) and downtime due to physical damage. These guidelines should be communicated throughout the company (and appropriate training should be provided to employees at all levels). In addition, companies should organize and maintain accounting files, and keep other important documents, such as copies of their insurance policies, in an accessible location, which will facilitate the preparation of insurance claims, including: (1) accounting guidelines for a disaster; (2) historical financial performance documents; (3) current financial forecasts with documented support; and (4) documentation reflecting the company's procurement process (e.g., a list of certified vendors). Equally important is understanding what types of losses are covered by the company's – and possibly other entities' -- various policies (including property insurance policies, commercial general liability policies, and environmental policies) such that cost control and recording can be categorized and allocated properly.

It is important for companies to maintain, in a secure location, an up-to-date inventory of their property and assets as well as photographs or video footage of their assets. This should help avoid or minimize potential post-loss disputes regarding the existence, number, or pre-loss location and condition of assets that were damaged or destroyed.

Finally, companies should be sure to take reasonable steps to avoid, or to minimize, impending losses. Property policies typically cover costs incurred to protect property from an impending loss, such as costs incurred to secure a facility before a forecasted severe weather event. The ER Manager, or another member of the Crisis Management Team, can coordinate such activities.

POST-DISASTER RESPONSE

After a loss occurs, a company should consider taking the following steps in order to efficiently and effectively address environmental concerns, while mitigating liabilities and maximizing the likelihood of recovery from the company's insurance carriers.

IDENTIFY, CONTAIN, AND CLOSE ENVIRONMENTAL HAZARDS

After a disaster, while the pre-approved response contractors are mobilizing, the ER Manager should first conduct a life safety inspection of the affected areas for hazards. Environmental, electrical, and structural hazards may need assessment by a licensed professional in some instances. The ER Manager will also photograph and videotape the entire affected area with an eye for "causation" of damage. Often photographs are focused on the results of the major damage as they can be startling. All areas affected should be photographed as there may be subtle clues to causation that will help in proving and negotiating insurance claim(s).

The ER Manager typically should immediately convene a meeting with the disaster team and a senior person from each response contractor on site to establish: (a) a chain of command, (b) communication channels, (c) a written scope of work, at least for the first 48-72 hours, (d) a written "resource loading" plan that matches the scope, and (e) a schedule, by shift and budget, in a simple Gantt chart format or a computerized Critical Path Method, cost-loaded project schedule.

With the correct project management expertise, these items often can be completed within eight (8) hours of arriving at the loss site. As the initial response unfolds with the objective of controlling environmental hazards, preventing electrical or structural damage causing fire or injury and removing free water, the ER Manager typically will continue to perfect the scope, schedule, and estimate for investigation and remedial measures needed to fully address the environmental hazards. The ER Manager will also typically will deploy his or her own staff to direct and oversee all contractors and vendors on every shift. In addition, the ER Manager can coordinate with insurance carriers or their adjusters to help them set reserve(s) for the claim(s).

The ER Manager should also be responsible for ensuring, to the extent possible or practicable, that all project documentation and reporting meet the requirements of not only regulatory agencies, but also of the insurance carrier(s) and claim adjustor(s). Each subcontractor must be instructed to keep records to substantiate the labor, consumables, and the time and amount of equipment run.

Assess, Quantify, and Pursue Coverage for Your Losses

The following post-loss steps should get the insurance claim adjustment off to the right start.

First, companies typically must provide written notice to insurance carriers. Carefully review your insurance policies, and, as soon as possible, provide proper written notice to all carriers that issued potentially applicable policies, such as first-party property insurance policies, commercial general liability policies, and environmental liability policies. Failure to give timely notice could jeopardize your coverage or result in a protracted (translation: costly) dispute about whether the carrier is off the hook.

Second, calendar all policy deadlines. Insurance policies generally, and property policies in particular, tend to contain requirements and deadlines for providing notice, submitting a proof of loss, completing repairs (in order to recover the replacement cost value of the damaged or destroyed property), and for filing a lawsuit against the carrier (if necessary). Some of these deadlines can be as short as 30-60 days from the date of loss. It is best to identify, calendar, and meet these deadlines, and to timely request extensions, in writing, when necessary.

Be sure to protect and to provide the carriers with evidence relating to the loss. Gather and preserve all documents that substantiate or relate to losses, such as photographs, video footage, invoices, receipts, and labor records. These documents will enable the company to prove damages and (hopefully) get the insurance claim paid. Additionally, most insurance policies contain some form of cooperation clause, which typically requires the policyholder to comply with insurance carriers' reasonable requests for information that will enable them to investigate and adjust the insurance claim(s). The company also may be required to preserve such information in connection with actual or anticipated litigation.

As soon as possible, develop a business recovery plan to return the company to full operations, which, from an environmental standpoint, typically can begin when the environmental response is substantially complete. Assess the impacts property damage is likely to have on business operations and financial performance. In order to develop and implement a plan to return to full operations, consider the following possible scenarios and options: (1) a full shut-down during the rebuild period; (2) a partial shut-down during the rebuild period; (3) alternate facilities to use during the rebuild period; and/or (4) use of outside vendors to help mitigate loss. The plan selected will impact the time it likely will take for the company to operationally and financially recover from the environmental disaster. The options and plan selected, and the estimated recovery time, should be communicated to and discussed with the insurance carriers.

When losses are large or complex, the insurance claim adjustment process tends to be lengthy. Policyholders should not be forced to fund their entire recovery in the meantime. Companies should request advances and/or interim partial payments for undisputed portions of the loss.

CONCLUSION

As illustrated above, there are many complex and varied issues involved in preparing for and responding to a disaster, and all likely will involve some element of anticipating, mitigating, and responding to environmental risk. A company will be best served by establishing early on a multi-disciplinary team to coordinate pre- and post-disaster activities in order to maximize the likelihood that it will quickly and fully recover from such a loss. This team approach will help minimize environmental exposures while positioning the company to maximize the likelihood of recovering insurance proceeds for its losses. The team needs to be led by an independent ER Manager that is aligned with the company, as opposed to the mitigation or response subcontractors. This ER Manager generally accepts responsibility for managing and completing the response in the timeliest and most efficient manner and for documenting the claim for ease of processing by, and securing payment from, the insurance carriers.