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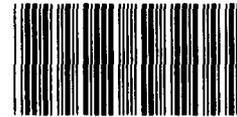
Report to the Chairman, Subcommittee  
on Policy Research and Insurance,  
Committee on Banking, Finance and  
Urban Affairs, House of  
Representatives

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February 1991

# HAZARDOUS WASTE

## Pollution Claims Experience of Property/Casualty Insurers



143072





United States  
General Accounting Office  
Washington, D.C. 20548

Resources, Community, and  
Economic Development Division

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February 5, 1991

The Honorable Ben Erdreich  
Chairman, Subcommittee on Policy  
Research and Insurance  
Committee on Banking, Finance and  
Urban Affairs  
House of Representatives

Dear Mr. Chairman:

On August 13, 1990, you asked us to testify on the potential liability of property/casualty insurers for costs of cleaning up hazardous waste sites. In preparing for our testimony at the Subcommittee's September 27, 1990, hearing,<sup>1</sup> we surveyed the pollution claims experience of 20 of the nation's largest property/casualty insurers. These insurers accounted for 67 percent of the total general liability market in 1989.<sup>2</sup> During the hearing we presented some preliminary results of this survey. This report provides more specific information on our survey results, as you requested.

## Results in Brief

Of the 13 responding insurers included in our survey, only 9 provided us with data on the claims they closed with payment in 1989. These nine respondents reported that they paid about \$106 million, or an average of about \$44,000, on the 2,393 claims they closed with payment in 1989. While only four of the nine respondents provided claim payment data for the 5-year period from 1985 to 1989, all four experienced a sharp increase in their average pollution payments during this period.

Responding insurers did not provide data on the reserves they had set aside to cover pending (open) and future pollution claims, as our survey requested. However, the large number of open claims (about 50,000) and pending lawsuits over insurance coverage for pollution liability (about 2,000) indicates that insurers may have much more at stake than their past pollution claims experience would otherwise suggest. Our survey

<sup>1</sup>Potential Liability of Property/Casualty Insurers for Costs of Cleaning Up Hazardous Waste Sites (GAO/T-RCED-90-109, Sept. 27, 1990).

<sup>2</sup>Pollution insurance is one of many forms of liability insurance in the property/casualty industry's "general liability" (or "other liability") line.

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further shows that in 1989 responding insurers spent about \$158 million, or an average of \$15.8 million per insurer, on lawsuits involving pollution coverage issues or claims against insureds by third parties.<sup>3</sup>

As we stated in our September 1990 testimony, the actual cleanup costs that insurers will ultimately have to defray will depend in part on the share of the nation's cleanup effort for which insurers are found liable under lawsuits. However, without a centralized source of data on the pollution claims experience of insurers, the magnitude of cleanup costs being absorbed by insurers will remain unknown.

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## Background

The Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA), more commonly known as Superfund, requires the parties responsible for contamination at the nation's worst hazardous waste sites either to clean up the sites themselves or reimburse the government for cleaning them up. The Environmental Protection Agency (EPA), which administers Superfund, currently has identified about 1,200 sites as eligible for long-term, permanent cleanup under Superfund.<sup>4</sup> The parties liable for these cleanups include present and past owners or operators of sites, all generators of hazardous waste found at the site, and certain transporters of these wastes.

In interpreting CERCLA's liability provisions, courts have consistently held that Superfund liability is strict and, where the harm is indivisible, joint and several. Strict liability means liability without fault. Under a strict liability standard, a responsible party may be held liable for cleanup costs regardless of the care it has taken to prevent contamination. Under the joint and several liability standard, one party may be held liable for all cleanup costs even if others contributed to the contamination. In theory, then, a single party may be threatened with potentially large costs.<sup>5</sup>

Given these liability standards and the millions of dollars often required to clean up a hazardous waste site—an average of at least \$29 million

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<sup>3</sup>Typically, general liability insurance policies call for the insurer to defend the insured in suits brought against the insured for damages covered by the policy.

<sup>4</sup>Sites not eligible for Superfund cleanup may be subject to cleanup under state programs.

<sup>5</sup>Joint and several liability applies in most cases because wastes have been commingled. But where the harm is divisible and a reasonable basis exists for apportioning costs, the responsible party will be held liable only for the portion of the harm that it caused.

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for a single Superfund site, according to EPA estimates—responsible parties are looking to their insurers to pay for site cleanups.

Before the 1970s, insurers provided coverage for a broad range of commercial liability resulting from accidental personal injury or property damage—which might have included pollution incidents—under comprehensive general liability policies. But as their awareness of the financial liabilities associated with pollution incidents increased, insurers began in the late 1960s to revise, redefine, and limit policy language that might apply to pollution damages. For example, a “pollution exclusion” clause was added to the standard comprehensive general liability policy to specify that the policy covered only sudden and accidental pollution incidents.

During the 1970s, insurers further revised their policies to better define their financial responsibility for pollution incidents. For example, some insurers developed entirely separate environmental impairment liability policies specifically to cover pollution risks. By the mid-1980s, though, most insurers had ceased to offer new insurance policies covering pollution-related damages.

Insurers withdrew from the pollution market for several reasons. Primarily, they contended that environmental legislation, as well as recent trends in common law and court interpretations of environmental law, had broadened their liability for pollution coverage beyond what had been intended under past policies. They maintained that this increased liability left them exposed potentially to enormous payments for claims presented under these past policies.

While insurers have acted to limit pollution coverage, disputes have arisen over the years between insurers and their policyholders over the extent to which their policies provided pollution coverage. In a 1987 report, we reviewed court cases involving these coverage disputes.<sup>6</sup> These disputes focused on key contract issues, such as whether an insurance contract’s pollution exclusion clause applies to the insured’s release and whether pollution cleanup costs are covered damages under the policy. At that time, we reported that the resulting court decisions varied, sometimes favoring the insurer and sometimes favoring the insured, with no trends emerging. In our September 1990 testimony, we stated that the extent of insurers’ obligations to pay responsible party cleanup costs remained undefined.

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<sup>6</sup>Hazardous Waste: Issues Surrounding Insurance Availability (GAO/RCED-88-2, Oct. 16, 1987).

## Insurers' Pollution Claims Experience

The nine respondents that provided claim payment data for 1989 reported that they paid about \$106 million, or an average of about \$44,000, on the 2,393 pollution claims that they closed with payment during that year. While our survey sought claim payment data for the 5-year period from 1985 to 1989, only four insurers responded with information for this entire period. As shown in table 1, the average pollution claim payments for these four insurers as a group more than quadrupled between 1985 and 1989. The number of pollution claims that the four closed with payment also more than quadrupled during this period. Individually, each insurer experienced a sharp increase in average pollution claim payments during this period, with average payments for 1989 ranging from three to eight times higher than average payments for 1985.<sup>7</sup> The experience of these insurers, however, does not necessarily reflect other insurers' claims experience or pollution liability exposure.

**Table 1: Claim Payments for Four Insurers (1985-89)**

Year	Number of claims closed with payment	Claim payments <sup>a</sup>	
		Total (in millions)	Average per claim
1985	176	\$2.7	\$15,600
1986	266	5.2	19,500
1987	241	5.6	23,400
1988	426	25.7	60,300
1989	786	51.4	65,400

<sup>a</sup>Total claim payments are rounded to the nearest hundred-thousand, whereas average claim payments are rounded to the nearest hundred.

The number of open claims and lawsuits in which insurers are involved indicates that insurers potentially have much more at stake than even their past claim payment experience would suggest. The 13 responding insurers reported that they had 49,947 pollution claims open at the time of our survey, not all of which will necessarily be closed with payment. Also, these 13 insurers reported that they were engaged in 1,962 lawsuits with insureds over pollution coverage issues. According to 10 of these responding insurers, these lawsuits involved about 6,000 hazardous waste sites. However, the number of lawsuits and affected sites is no doubt inflated because such suits can and do involve multiple insurers for the same site.

Insurers also reported that they had incurred millions of dollars in legal costs in pursuing these lawsuits and in defending insureds against third-

<sup>7</sup>These four insurers accounted for about 11 percent of the premiums written for general liability insurance in 1989.

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party claims. In 1989, according to our survey, 10 responding insurers spent about \$158 million, or an average of \$15.8 million per insurer, on lawsuits over pollution coverage issues or involving the defense of insureds against third-party pollution claims.<sup>8</sup>

While our survey also sought information on the reserves insurers had set aside to cover both open and expected future claims, none of the 13 responding insurers provided this information. An attorney representing seven of the respondents stated that these insurers did not believe that their policies provide coverage for Superfund cleanups or for many other environmental claims. This attorney also stated that any reserves these companies may have established reflect a variety of management policies and perceptions and are of no general significance to pollution claims.

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## No Centralized Record of Pollution Claim Payments Exists

Cleaning up this nation's hazardous waste sites will cost billions, or possibly hundreds of billions, of dollars, according to estimates by insurers, federal agencies, and others. How much of these cleanup costs insurers will ultimately have to absorb will depend, as we stated in our September 1990 testimony, on (1) the size of the nation's cleanup effort, (2) the share of this effort that responsible parties will fund, and (3) the share of this effort for which insurers are found liable under coverage lawsuits. However, without a centralized source of data on the pollution claims experience of insurers, the magnitude of cleanup costs being absorbed by insurers will remain unknown.

We first noted the absence of a centralized, comprehensive data source on pollution claim payments in our 1987 report to the Congress entitled Hazardous Waste: Issues Surrounding Insurance Availability (GAO/RCED-88-2, Oct. 16, 1987). In that report we suggested that the Congress consider requiring insurers or responsible parties, as appropriate, to report to EPA the amounts of pollution claim payments made to cover cleanups and other expenses relating to these claims.

In our September 1990 testimony, we noted that centralized information on the pollution claims experience of insurers is still not available. We therefore reiterated our 1987 suggestion that this information be collected to aid congressional policy-making in this area.

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<sup>8</sup>Some of the legal costs for defending insureds may have been included in the \$44,000 average pollution claim payment that responding insurers made on the claims they closed with payment in 1989.

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## Conclusions

Average claim payments for some survey respondents increased sharply between 1985 and 1989. Also, the large number of open claims and lawsuits involving pollution coverage issues suggests that responding insurers could be faced with substantial claim payments in the future. The millions of dollars that responding insurers spent in 1989 on these lawsuits and on the defense of insureds is further evidence of the magnitude of the pollution claim problem insurers could face.

Unfortunately, no centralized, comprehensive data on the pollution claims experience of insurers are available. For this reason, we suggested in both our October 1987 report and our September 1990 testimony that, to remedy this problem, the Congress may want to require insurers or responsible parties to report the amount of their pollution claim payments to a central source.

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Our survey was conducted during September and October 1990 in accordance with generally accepted government auditing standards. Appendix I contains information on our survey objectives, scope, and methodology.

As arranged with your office, copies of this report are being sent to appropriate congressional committees; the Administrator, EPA; the Director, Office of Management and Budget; and other interested parties.

Major contributors to this report are listed in appendix II. Please contact me at (202) 275-6111 if you have any questions.

Sincerely yours,



Richard L. Hembra  
Director, Environmental Protection  
Issues



# Objectives, Scope, and Methodology

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Our survey of insurers was designed to obtain data on (1) the pollution claims that insurers closed with payment from 1985 to 1989 on their comprehensive general liability and environmental insurance liability policies, (2) open claims, (3) available reserves for open and future claims, (4) lawsuits involving pollution coverage issues, and (5) legal fees resulting from these suits and suits involving the defense of insureds against third party claims. Our survey was initiated in response to a request from the Chairman of the Subcommittee on Policy Research and Insurance, House Committee on Banking, Finance and Urban Affairs, to testify on the potential liability of property/casualty insurers for costs of cleaning up hazardous waste sites.

We selected the 20 property/casualty insurers for our survey on the basis of the dollar amount of direct premiums they wrote for general liability insurance in 1989, as reported by A.M. Best Company.<sup>1</sup> We limited our review to general liability (other liability) insurance because most pollution coverage comes under this category. Also, we limited our survey to the 20 largest insurers in hopes of completing this limited survey in time to include its results in our testimony.

In all, we received responses from 14 insurers, or a 70 percent response rate. However, we did not include one insurer's response in our survey results because this insurer provided estimated rather than actual claim payments. The 13 responding insurers included in our survey results accounted for about 49 percent of the total general liability insurance premiums written in 1989. Only 4 of the 13 insurers provided claim payment data for the full 5-year period. We could not verify survey responses because insurers consider their claim files to be confidential. Furthermore, given the number of insurers surveyed and the number of responses received, our survey results do not provide a statistical basis for making projections.

Our survey was conducted during September and October 1990 in accordance with generally accepted government auditing standards. Participation in our survey was voluntary since we do not have authority to require the insurers to respond. To encourage a good response rate, we extended a formal pledge of confidentiality to the insurers, promising that we would report only summaries of aggregate data.

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<sup>1</sup>A.M. Best evaluates and rates insurance industry financial performance.

# Major Contributors to This Report

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