Chubb Environmental Advisory

Meeting the Challenges of Enviromental Risks in International Construction

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The U.S. construction industry is taking on a more international flavor as more domestic contractors bid, and win, projects abroad. From oil pipelines in western Canada to infrastructure projects in South America, U.S. embassies in various European countries, U.S. contractors are welcoming the opportunities to work in new countries. While they deal with the cultural and legal differences of foreign projects, contractors should not overlook the significant risks that the varying environmental regulations in each country may pose for the project and for their company.

Before they embark on international projects, contractors should assess the environmental regulations in those countries to make sure that their construction work will comply with local laws and customs. They should also review their insurance program to determine if it can provide the coverage needed in the new locations and whether they will need local insurance coverage and claims handling capabilities. When considering international projects, contractors should seek to work with a carrier that has a strong international presence as well as a deep understanding of the construction industry and environmental risks.

Global Economic Growth Increases Construction Demand

For the construction industry, the growing international demand for new buildings and infrastructure presents a significant opportunity. As the economies of developing nations mature, they need to meet the needs of a rapidly growing middle class.

Globally, the middle class will grow to 4.9 billion people in 2030 from 1.8 billion in 2009, the OECD estimates. Most of that growth will occur outside Europe and North America in developing countries' metropolitan areas.[1] About $57 trillion in infrastructure investment will be needed globally through 2030 just to keep pace with economic growth, the McKinsey Global Institute estimated in 2013.[2]

South America provides a good example of the growing investment in infrastructure. Colombia, for instance, has embarked on a $24 billion highway construction program to help boost economic development.[3] As Latin American countries take a larger presence on the world stage, they also are investing in prestige events. For the 2014 World Cup, Brazil invested more than $11 billion in infrastructure, including the

construction of new stadiums around the country and the renovation of existing ones.[4] Brazil has projected infrastructure spending of $2.3 billion for the 2016 Rio de Janeiro Olympics, but that total was seen as likely to rise.[5]

While emerging economies seek to improve their infrastructure, developed nations continue to take advantage of global opportunities. For example in western Canada, energy-related projects remain a key focus. In June 2014, the Canadian government approved a $7.3 billion pipeline project, which will transport oil from Alberta to the West Coast for final export to Asian markets.[6]

Already, construction forms a significant contribution to global trade. World construction exports rose 4.5 percent to $115 billion in 2012, the World Trade Organization reported. Major importers of construction services include the European Union and Russia; China, South Korea and Japan in East Asia; Saudi Arabia in the Middle East; and Angola and Algeria in Africa.[7]

Economic Growth Heightens Environmental Awareness

Along with the economic changes, the growing global middle class means that millions more people are focused not only on meeting basic needs but also on protecting the environment. China, for instance, has placed a greater emphasis on protecting the environment and addressing pollution issues that accompanied its rapid growth over the last few decades. In 2014, China amended its environmental protection law for the first time in 25 years, setting tougher penalties for pollution infractions.[8] The amendments, which are to take effect January 1, 2015, would allow fines based on the length of time illegal pollution occurs, rather than one-time penalties, and would permit approved non-governmental organizations to bring lawsuits over pollution.[9]

As the economies of Latin American nations grow, those countries are also showing an increased focus on environmental stewardship. For instance, Mexico adopted a comprehensive law in 2013 establishing guidelines for environmental liability and civil actions.[10]

Developed nations continue to tighten their own environmental standards. The European Union has adopted a bloc-wide approach to environmental regulation under its Environmental Liability Directive. The Directive establishes a framework based on the "polluter pays" principle and covers damage to land, water, protected species and natural habitats. The Directive extends beyond primary remediation to biodiversity damage and may require damaged natural resources to be restored or equivalent resources to be created. Restoration projects may be expensive and measured in years rather than months. While the Directive sets out a common framework, European member states take varying approaches and some have enacted stricter regulations.

International Considerations May Complicate Insurance Coverage

As U.S. contractors consider international projects, they need to assess the impact that national laws concerning both the environment and insurance may have on their exposures. Some countries may require environmental insurance coverage with set limits, while others may leave it to the discretion of the contractor. Environmental insurance could be a contractual requirement for the project, but the contractor still needs a thorough understanding of that particular country's insurance regulatory requirements.

Contractors should be aware of how international conditions change the approach to insurance. In the U.S., contractors pollution liability insurance serves to fill in gaps in coverage resulting from pollution exclusions in general liability policies. The focus on liability coverage is a reflection of the heightened risk of litigation in the U.S.. In Asia, general liability is not a standard coverage, and property policies are more typical. Property policies, however, are also likely to exclude pollution risks. In many foreign countries, liability may not be the major risk, but rather a pollution incident that requires an expensive on-site remediation that halts work for a long period of time.

A convenient solution would be for U.S. contractors to rely on their U.S.-based policies to cover environmental risks in other countries, but that is not possible in many cases. A number of countries require insurance policies to be issued by a local insurer licensed to do business in that country. The requirements for such locally admitted insurance may vary by territory within a single country. In Canada, some provinces require that insurance policies be issued by a locally admitted insurer, while other provinces do not. Some countries may allow "non-admitted" coverage in theory, but in practice make it very difficult or expensive to use or to place.

In addition, countries such as Italy require claims to be handled locally. In those cases, U.S.-based insurance policies may not be able to pay claims locally. Contractors with foreign policies not only run the risk of being unable to have local payments made on their behalf for claims, but also open themselves up to potentially significant tax complications.

Besides local legal considerations, contractors should recognize that coverage may be difficult to obtain for projects in very remote areas, or that U.S. law may preclude U.S. insurers from providing coverage in certain regions or countries.

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Setting a Global Standard for Environmental Safety

While each project presents its own challenges, environmental risks remain generally similar. Common environmental exposures arise from construction operations and include spills of fuels or chemicals or other damage to the local natural environment, for example, oil washed away from road construction during a rainstorm and resulting in site runoff. Other risks stem from construction materials native to a particular country, materials brought onto the site, and transportation of construction materials and waste.

Those risks may be heightened in foreign countries by local infrastructure, customs and regulations. A lack of well-maintained roadways may not only make it more difficult to bring supplies to a project, but also may increase the environmental hazards associated with transporting materials. Waste disposal may present another challenge if the sites are substandard, loosely regulated or if enforcement is lax.

Inadequate safety and protective equipment may create health and environmental problems. Local work practices may be an issue if they increase pollution or safety risks. When it comes to hazardous materials, workers may not be familiar with handling procedures that are standard in the U.S.. Cultural issues also need tobe addressed to avoid inadvertently alienating the local workforce, which could result in heightened environmental and safety risks.

Local laws may also present challenges. To ensure compliance, contractors should thoroughly evaluate the regulations governing the entirety of the project, from permitting through completion. Besides assessing the existing local regulations, companies need to understand how those laws are enforced in practice. Contractors should be mindful of any pending laws that could come into force while the project is underway.

When it comes to the project itself, contractors should seek to institute the same rigorous environmental practices that they apply domestically. This helps to demonstrate a strong commitment to environmental stewardship to the local community and regulators. Adequate environmental insurance is a key part of this approach as it helps to ensure that any incident can be handled in a way that minimizes environmental damage.

While the overall risks may be similar, contractors may face environmental issues that are not common at home. In nations such as India, for instance, contractors may find that some forms of asbestos are still commonly used in construction, even though personal injury claims for asbestos-related injuries in the U.S. have run into the billions of dollars.11 Contractors also may run into issues such as lead-contaminated soil in countries such as Algeria, Yemen and Iraq where leaded gasoline has remained in use as of 2009.[12]

Making the Environment a Key Focus

Because environmental risks may be complicated by local issues on international projects, contractors should make sure that they take the insurance implications into consideration from the start, including contractual obligations. For instance, they should be aware of contractual terms that could hinder their ability to obtain adequate risk transfer. For that reason, contractors should work with their brokers and insurers early in the process.

Contractors may want to seek risk engineering advice to help evaluate the environmental risks associated with a given project. This should include current and proposed regulations in the country. Risk engineers can help to identify potential exposures on a site and areas where special training may be required. They also can help contractors educate local subcontractors and their workers on the company's safety and environmental procedures.

When it comes to risk transfer, contractors should understand where they can use a global insurance program and where they will need locally issued policies and services. For that reason, they should work with an insurer that can provide both global and locally issued insurance policies, along with local claims handling capabilities and engineering services. The insurer should have local affiliated companies or established relationships with local insurer partners, and understand the country's culture. Contractors working in a number of countries may want to consider a global master program in their home market that also provides locally admitted policies where required.

International opportunities can open up new avenues of growth, but U.S. contractors should be aware of how the environmental risks may change across borders. Addressing these exposures from the very start of a project and working with a carrier that understands the industry and the risks, are key steps in a successful international project.

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