Guest Editorial

Climate Liability Risk: Will it be the Next Chapter in the Global "Blame Game"?

by Richard H. Murray[+]

It has long been accepted that the "compensation culture" that arose in the U.S. about 40 years ago has in this century taken on global dimensions.

A simplistic but accurate description of a compensation culture is a society in which most injuries can be traced to a causal agent from whom damages for the harm may be recovered.

The history of the relationship between injury and compensation may be briefly summarised in four stages.

- The pre-Industrial Revolution era of *"caveat emptor"*—the longstanding principle that injuries occurred without recourse. The concept may offend our sensibilities today, but it was consistent with the economic model and social norms of the many centuries in which it ruled. Life in those times was harsh, and one protected oneself from others as best one could.
- *Caveat emptor* proved a poor vehicle on which to spread commercial activity, far beyond the communities of production. The common law jurisdictions (primarily the English-speaking British Empire) fostered commerce by creating what we came to know in the 20th century as the civil justice system, encompassing "tort law" that awarded damages to those owed a duty of care by those who injured others through negligent breach of that duty. The civil law jurisdictions, with roots in continental Europe, supplied compensation for injury through statutory schemes that generally awarded less than the common law, but set no requirements of proving breach of duty or causation. Both systems supported the commercial needs of the last century.
- As life became generally more sheltered, and the comforts expected by the growing middle class gained political influence, a "compensation culture" emerged that demanded wider and better payment for all manner of injuries, including pain, suffering and behaviour-controlling penalty damages. The existence of liability insurance facilitated these movements. In the U.S., the last second half of the 20th century saw the standards of the civil justice system eroded to add a dimension of wealth transfer. Those operating under civil law schemes found the demands for compensation exceeded the state's ability to pay, leading to various forms of transferring liability schemes onto the private sector and their insurers.
- The new century has been stunned by the frequency and severity of weather-related extreme events which have been partly attributed to climate change and in turn to the emission of greenhouse gasses into the atmosphere. The sharp escalation of widespread suffering and the decades of frustration by those concerned about the effects of global warming have introduced a new era best described as "The Blame Game"—a search for those who could be punished for contributing disproportionately to CO_2 emissions through use of liability claims or criminal prosecution. The two remedies often operate in tandem.

Liability law has thus seen a remarkable set of transformations in a short time. From no compensation for injuries caused by others *(caveat emptor)* we have moved through successive phases of liability for economic loss where the negligent cause was clearly demonstrable (Civil Justice) and then wealth distribution by generous liability for pain, suffering and exemplary damages (Compensation Culture) to the socialisation of losses caused by natural causes (The Blame Game).

At each stage of this evolution the causative forces have been similar: economic, political and social. Each has had its turn of dominant influence. The needs of commerce demanded that buyers receive some protection from distant and unknown sellers. With the rise of the middle class, the scope and amount of available compensation became a political priority. Most recently, the magnitude of human suffering, communicated visually around the world via television and the internet, has stirred passions

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of sympathy and anger that must be assuaged. At each of these mileposts, it has been the creativity of the legal profession and the pressures on the judiciary that have enabled shifting legal standards to accommodate necessity via liability law.

These are essential conditions for insurers to understand today, because the pace of change has accelerated, the period of latency between event and injury has shortened and the law has grown comfortable with the retroactive application of rules that ease and amplify recovery. For insurers, the result is the ever greater frequency of retrospective application to insurance. A contract of insurance is formed at a point in time, with the price of coverage set by the known exposures of the day. When those exposures are enlarged by shifting legal standards prior to the maturing of latent claims, the cost of the promises contained in the contract rises without commensurate increase in the previously paid premium. One need only consider the painful history of asbestos insurance claims to recognise the risks embedded in the blame game.

We are in the very early days of the blame game. But manifestations of it are evolving rapidly. We consider first the use of criminal law.

Stephan Schmidheiny is best known to the world as a passionate supporter of environmental protection. He was the founder of The World Business Council for Sustainable Development and co-organiser of the 1992 Earth Summit in Rio de Janeiro. Mr Schmidheiny is unrivalled in green credentials. He is also a member of a very affluent Swiss family with a wide variety of business interests including an Italian asbestos producer. When Mr. Schmidheiny became Chairman of that company's Board he ordered the discontinuance of asbestos manufacturing, all of which was ended and cleansed by 1986, six years before Italian regulation banned asbestos manufacture. None of this prevented the Italian government from launching a criminal prosecution against Mr Schmidheiny for personally contributing to asbestos-related injuries and deaths attributed to the company's prior decades of production. In February of 2012 he was convicted and sentenced to a 16-year prison term and a fine of €100 million. His business partner, the Belgian Baron de Cartier de Marchienne, was sentenced to the same punishment. Italy had found a headline-generating and affluent target of blame.

Italy is equally willing to blame Italians. The country established a "Major Risks Committee" of leading scientists to advise on earthquake risks. One would have seen this as a prestigious assignment. Seven members of the Committee might now doubt the value of such prestige. In the spring of 2009 they were asked to advise whether minor trembles in the vicinity of L'Aquila, a medieval town in Abbruzzo, warranted evacuation of the region's population. The experts concluded that evacuation of such massive scale was not warranted. Six days later a major quake struck, killing hundreds. There are no known errors or omissions in the Committee's work, the prediction of seismic events not yet being a science. Nevertheless the seven scientists were indicted on manslaughter charges. The trial began in late 2011 and the ruling is expected for summer 2012.

Hopefully these will remain rare uses of criminal charges to establish blame. But the application of blame-based civil liability claims is more frequent and growing. The following are a few illustrations:

- In the U.S., numerous liability claims seeking damage recoveries have been filed against power companies and other greenhouse gas (GHG)-emitting industries, based on new applications of the old principles of nuisance and public nuisance—principles developed in the common law to address disputes between neighbours. The most noted involves a suit against American Electric Power Company which reached the U.S. Supreme Court in 2011, on the question of whether nuisance principles would support the recovery of damages for climate-related extreme events. In a decision that is unclear in many respects, the Court did declare unanimously that such claims could be brought on nuisance theories in state courts. U.S. claims are also exploring the adaptation of negligence theories for placing climate risk blame—and liability.
- Negligence theories are being explored in the U.K. as well. It has been proposed, for example, that liability should be imposed on all who were responsible for the development of flood plains exposed to climate-related extreme events, whether caused by wind and rainfall or the rise of ocean levels.
- Sea level rise is at the heart of many proposed forms of new liability theories. The prospects for a complete loss of the low lying nation state of the Marshall Islands has attracted much attention. With assistance from The Center for Climate Change Law at Columbia University, U.S.-based attorneys for the islands have lodged a complaint with the Czech Republic on the

grounds that it commissioned Europe's largest coal-fired power plant on the basis of a flawed Environmental Assessment Study. The alleged flaw is the failure to have considered the plant's impact on accelerating the drowning date for the Marshall Islands. Such an assertion has all the hallmarks of a precursor to a liability claim of great magnitude for the destruction of a nation.

Other examples of newly conceived forms of blame and consequent liability abound. But their number and particulars are of less importance than the fact that this pattern of "blame and sue" is becoming commonplace.

Most such claims will fail in their first endeavour. But so did all the early tobacco and asbestos claims. The time between the initial assertion of new tobacco and asbestos claim theories and the first success by settlement was several decades. The blame game has accelerated in relation to climate-related liability, where the first settlement arose out of Hurricane Katrina and occurred four years after the first claim assertion.

The social order of this new century no longer tolerates injury without searching for those to blame and from whom recovery may be had. The search focuses on the sources from which substantial recovery can be obtained. Those two objectives are intertwined. For recovery to take place, we still require a connection between the harm and a target of blame that satisfies today's cultural norms. But those norms are easily satisfied. So the availability of resources for obtaining recovery becomes a factor in assigning blame. There would be no reason for the Marshall Islands to sue Inuit Indians for their contribution to CO_2 emissions, since they have little resource and are themselves seeking a blame and recovery source from the energy industry for their relocation woes. Blame and liability tend to converge at the deepest asset pools, as Stephan Schmidheiny discovered.

The implications of this convergence for insurers are significant:

- A study conducted for UNEP FI by the consultancy TruCost estimated in 2011 that the annual average cost of climate-related extreme events is US$6.6tn, of which over US$2tn annually is attributed to human activity. The study then compared that amount to the profits of the world's 3,000 largest for-profit companies. The circuitry for potential blame and liability is thus identified.
- With the hardship of climate-related damage often falling on the least developed economies, situated in the Southern Hemisphere, and far exceeding available property insurance and public sector resources, the search for additional sources of recoveries via liability claims will be fuelled by powerful humanitarian impulses and mostly fall onto economic actors in the Northern Hemisphere.
- The innovative application of liability theories and the inevitable carbon footprint of all industries threaten insurers with exposure to liability claims that will be pervasive and difficult to avoid through traditional exclusionary clauses.
- Liability claims have a longer latency period than property insurance, exposing insurers to the future lowering of legal barriers with retroactive effect, a condition that was painfully recognised in asbestos claims.
- As social and economic forces carve new channels of accepted liability theories to foster the humanitarian urgencies of windstorm damage, those theories could easily migrate into other aspects of liability exposures well beyond their direct application to climate claims.

The blame game and the ancillary liability issues provide insurers with opportunities for revenue generation through new resiliency-based products, and for demonstrating the value of insurance expertise and pricing tools for the benefit of all. Those opportunities are significant and important. But the blame game and its heritage need to be anticipated and understood as a 21st century phenomenon if insurance is to escape a liability tsunami before the opportunities can be explored.