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From Compliance to Sustainability:
Managing Multinational Environmental Exposures

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Executive summary

As more and more U.S. companies enter the global marketplace, complying with environmental laws can become a time-consuming and difficult task. Not only are there a vast number of laws already in effect across the world, the environmental law landscape is constantly changing. Furthermore, societal and business trends throughout the world increasingly compel businesses to adhere to environmental, health and safety standards that sometimes are more rigorous than those imposed by law.

Ensuring compliance with environmental laws may be costly and time-consuming, but a growing number of organizations are recognizing that a focus on sustainability, which goes beyond simple compliance, can result in competitive advantages. While often requiring significant effort, a systematic and sustained focus on environmental responsibility will not only help companies comply with the multitude of applicable laws , but may also enable them to reap benefits ranging from lower production costs to improved public relations, and can help them be more competitive in a globalized business environment.

Introduction

Environmental laws across the world are trending towards more, not less, regulation. The European Union is leading the way with expansive new directives, notably the Registration, Evaluation, Authorisation and Restriction of Chemicals (REACH) Regulation. Environmental standards tend to rise with per capita income,[1] and emerging economies increasingly are enacting and enforcing environmental regulations. In China, for example, environmental laws that were enacted over the past thirty years are being strengthened, and new environmental regulations and standards are being issued almost daily.[2]

Given the globalization of commerce and the nature of global supply chains, environmental regulations in one country or region can have profound implications for companies throughout the world. Companies with operations in foreign countries are subject to the environmental laws of that country. Increasingly, however, environmental laws apply to other aspects of commerce, and are even able to affect companies with no physical presence in a particular country. Typically these laws concern materials used in products. The EU's Restriction of Hazardous Substances (RoHS) Directive, for example, limits the use of certain hazardous substances in electrical and electronic equipment sold in Europe.

An international firm, with production facilities or products exposures throughout the world, can be subject to hundreds of local and supranational environmental laws that enhance the complexity of business management and compliance. The environmental compliance issues facing one global manufacturer of various metal machinery products are typical of those facing multinational manufacturing firms. The company lists on its website various environmental laws with which it states to be compliant:

- The Green Purchasing Law (Japan, voluntary compliance with standards)
- Toxic Substances Control Act (TSCA) (USA)
- California Proposition 65 (USA)
- RoHS (EU, with similar legislation in China, South Korea, Serbia and Ukraine)
- REACH (EU)
- Energy-related Products (ErP) Directive (EU)
- Waste Electrical and Electronic Equipment (WEEE) Directive (EU, with similar legislation in South Korea)

In many countries violations of environmental laws can result in criminal sanctions, restitution, performance remedies and civil penalties.

These are just some of the more significant laws, primarily dealing with product requirements, with which the company must comply.

Even in developed economies with well-established regulatory regimes, full compliance with environmental regulations is a challenging goal. The consequences of non-compliance, however, can be severe. In many countries, violations of environmental laws can result in criminal sanctions, restitution, performance remedies and civil penalties. The most significant financial liabilities for companies are those associated with clean-ups and penalties for breaches of regulations. The challenges of achieving and maintaining compliance with environmental laws can be daunting for multinational companies, but the need for compliance has never been greater.

Furthermore, legal compliance alone is no longer viewed as the end game by many companies. "Industry is on a three-stage journey from environmental compliance, through environmental risk management, to long-term sustainable development strategies," according to the International Institute for Sustainable Development.[3] A growing number of companies have found that a dedicated focus on managing their environmental risks – going beyond legal compliance and making environmental stewardship an integral part of their overall corporate strategy and management program – can produce tangible financial benefits such as product and process innovation, lower costs and improved product quality.[4] A reputation for environmental responsibility also can be a badge of good corporate citizenship, producing positive marketing and public relations benefits.

Risk management strategies

Compliance with environmental laws and standards can be a challenge even for a company doing business in a single country. The complexity of achieving compliance grows as companies expand beyond their home countries. An organized, systematic approach to compliance and environmental responsibility can ultimately save companies time, money, and lower the risks of non-compliance.

Use experts

Companies should seek out expert advice, beginning with a law firm or consultant experienced with the environmental laws in the countries in which the company operates. Consultants knowledgeable in local environmental laws and standards can be retained to audit facilities for compliance, provide invaluable input when acquiring operations in foreign countries, and audit suppliers in distant locations.

Engage suppliers who prioritize environmental risk management

Many companies are looking to reduce the environmental impact of their business processes, including their supply chains. Beyond the business and environmental benefits that can be achieved by promoting suppliers to do more to quantify and manage their environmental impacts, companies need to ensure that procurement standards comply with various countries' environmental laws and regulations. As a result, companies find themselves working with suppliers to collect more compliance data than ever before.

Several information systems developed by industry sectors are being used to obtain and communicate information on substances in articles. One vendor, for example, states that its product will "expedite the collection of chemical substance information and allow more efficient communication of information up and down the supply chain."[5] Increasingly, manufacturers require their suppliers to utilize one of these systems to identify and manage compliance with product environmental regulatory requirements. Additionally, components often are tested for compliance (a requirement under some regulations, such as RoHS).

Some industries, most notably the chemical industry, have developed voluntary environmental standards that will help companies achieve compliance.

Furthermore, to comply with product-related environmental regulations, some companies require their suppliers to operate in a safe and environmentally responsible manner. A growing number of companies are employing supplier management programs to assess supplier compliance with environmental, health and safety (EHS) standards. Risk-based assessments and self-assessment EHS questionnaires enable companies to identify and prioritize supplier risk. Suppliers identified as high risk are subject to on-site audits, often by third party auditors with local expertise. An integrated corrective action management approach is used to assure that any deficiencies are corrected in a timely fashion.[6]

Adhere to accepted standards for environmental management

Environmental laws around the world may have fundamental similarities. Adhering to widely-accepted voluntary standards will benefit companies in achieving compliance with laws across the globe.

A key environmental governance best practice is implementing an Environmental Management System (EMS), a framework for managing an organization's environmental programs in a comprehensive, systematic, and well-documented manner. ISO 14000, a family of standards addressing various aspects of environmental management, includes ISO 14001, the dominant EMS in the world. The EU Eco-Management and Audit Scheme (EMAS) is another EMS that has been widely adopted by European companies. The implementation of a robust EMS should lead to improved environmental performance, including better and more consistent legal compliance.

Some industries, most notably the chemical industry, have developed voluntary environmental standards that will help companies achieve compliance. Responsible Care is a voluntary global program to help chemical manufacturers and related businesses meet or exceed the compliance requirements of environmental regulations, and to achieve continuous improvement in health, safety and environmental performance. RC1401, a technical specification developed by the American Chemistry Council, is based on ISO 14001 and has been expanded to address the Responsible Care Principles.

Beyond assisting with legal compliance, the rigorous implementation of an EMS is an important step on the road to sustainability – creating products and employing processes that are not harmful to the environment and do not deplete natural resources. As previously noted, companies with a strong focus on environmental stewardship have been shown to often reap benefits ranging from lower production costs to improved public relations. A study by consultant A.T. Kearny found that, during the recent economic slowdown, companies that showed a genuine commitment to sustainability outperformed their peers in the financial markets.[7]

Insurance

Environmental insurance is an important coverage for companies in many sectors. Not only is it a smart discretionary purchase for companies with environmental exposures, it is mandatory in certain countries.

Structuring an insurance program that provides adequate protection to a multinational company presents a number of choices. There are three basic options for a multinational company to structure a global environmental insurance program: (i) separate, unrelated environmental policies issued and underwritten by local carriers in each country where the multinational company has exposure; (ii) a single global environmental policy issued in the multinational company's home country; or (iii) a controlled master program (CMP) which combines multiple primary local policies issued in various countries with an excess global master policy issued in the multinational's home country. Depending on the needs of the multinational company, the CMP may be the best option as local policies may aid in compliance with each country's particular regulations concerning requirements for locally admitted policies as well as help to avoid potential claims, tax and proof of insurance issues. The global master policy often serves as a backstop to the local policies by providing coverage where a local policy does not because of exhaustion of limits or a difference in conditions. Further, the global master policy may provide coverage for exposures that are not covered on any local policy.

For companies operating outside of their home countries, the risk of liability under foreign environmental laws is a recognized part of doing business.

Insurers should have the resources to implement effective pollution coverage on a worldwide basis. A global environmental insurer should not only have subsidiaries throughout the world that can issue local policies, or a network of affiliated local companies, it should have experts who are able to effectively manage complex environmental claims wherever they occur. Michelle Clark, Vice President of AIG's Environmental Division observes that, "By partnering with an insurer that has worldwide expertise and capabilities, clients can benefit from a compliance standpoint as locally issued environmental insurance may be required by law and from a claims standpoint as these insurers may have claims adjusters with experience handling environmental claims in numerous jurisdictions world-wide." Partnering with an insurance company that has a global claims department that handles a wide variety of claims, from the routine to those with heightened complexity, is critical in helping clients efficiently and effectively manage the overall claims process. An additional benefit of working with carriers who have global claims experience is that the carrier may also have relationships with emergency and crisis response firms, legal firms, technical experts, mediators, environmental consulting and remediation firms, forensic specialists and other resources around the world to assist with the adjusting process.

Multinational companies should also enlist the aid of a broker with broad experience in international environmental insurance issues, who can help them understand their global environmental exposures, and who understands and can explain the advantages and disadvantages of various structuring alternatives.

The global compliance challenge

Environmental laws and regulations range from municipal codes for disposal of certain substances to broad and encompassing national and supranational laws such as the TSCA and the Resource Conservation and Recovery Act (RCRA) in the U.S. and the Environmental Liability Directive (ELD) 2004/35/EC and REACH in the EU.

Companies with facilities in a particular country are subject to the laws of that country. Some countries have highly developed regulatory regimes and histories of strict enforcement of environmental laws. However, even in countries where environmental law compliance rates are low, foreign companies should not assume that they will avoid regulatory scrutiny and enforcement actions. In some countries such as China, enforcement of environmental laws against local companies often is lax, but foreign-invested entities are likely to be among the first targets for increased enforcement attention. Foreign-invested firms are often viewed as having deep pockets and therefore the means to bring their operations into compliance with the law. In addition, in China there is a general, though largely mistaken, perception that foreign companies are the worst offenders of the country's environmental laws.[8]

For companies operating outside of their home countries, the risk of liability under foreign environmental laws is a recognized part of doing business. But even companies whose operations are located entirely within their home country may face the risk of liability for violations of foreign environmental laws. Air and water easily travel across borders, sometimes carrying pollutants from one jurisdiction to another. Canadian companies that have been sued in U.S. courts for pollution that has migrated across the border can attest to the reality of this exposure.[9]

REACH, a European Community Regulation on chemicals and their safe use, is the largest and most comprehensive environmental regulation in the world. It came into effect in June 2007, and is to be phased in over 11 years. According to the European Commission, "The aim of REACH is to improve the protection of human health and the environment through the better and earlier identification of the intrinsic properties of chemical substances. The REACH Regulation gives greater responsibility to industry to manage the risks from chemicals and to provide safety information on the substances."[10] Any company that manufactures or sells products that pass through the EU at any point in their lifecycle are subject to REACH compliance.[11] Ultimately, any company seeking to do business in the EU will be required to comply with this regulation.[12]

In a growing number of cases, compliance with environmental standards is enforced not only by regulators, but also by customers.

In a growing number of cases, compliance with environmental standards is enforced not only by regulators, but also by customers. Some companies are being required by customers to meet environmental requirements even more stringent than those required by law. The Japan Green Procurement Survey Standardization Initiative (JGPSSI), for example, established standards that were considered voluntary, but many Japanese customers now require upstream suppliers to adopt the chemical management systems requirements and to push them throughout their supply chain.[13]

Beyond compliance: sustainability

A methodical and rigorous approach to environmental governance has benefits beyond complying with environmental regulations.

The ultimate goal of many companies with a strong environmental focus is sustainability. The U.S. Department of Commerce defines “sustainable manufacturing” as “the creation of manufactured products that use processes that minimize negative environmental impacts, conserve energy and natural resources, are safe for employees, communities, and consumers and are economically sound.”[14]

Studies have demonstrated that companies with a strong emphasis on sustainability not only are in a position to capitalize on a growing consumer preference for environmentally friendly products, they also often benefit from changes in materials and processes that both lower the environmental footprint and reduce overall costs. Among the cost savings are reductions in, or elimination of, end-of-pipe treatments as well as other costs of regulatory compliance as toxic substances and hazardous wastes are removed from manufacturing processes.

A.T. Kearney notes that sustainability means different things to different companies, ranging from transformational initiatives that are deeply embedded in the overall corporate strategy to more tactical environmental initiatives. Kearney also notes that the companies that achieve the greatest benefits are those that show a “true” commitment to sustainability.[15]

Conclusion

Because of a growing focus on green products and environmental stewardship, many firms must navigate through the thicket of environmental regulations to achieve legal compliance. As the world grows smaller and companies of almost every size pursue business opportunities outside their home countries, compliance issues multiply. As a method to manage environmental compliance, companies should develop repeatable and thorough processes including using experts to research and advise on environmental laws, aiming to work with suppliers who prioritize environmental risk management, improving compliance through adherence to widely accepted standards and partnering with insurance brokers and carriers who specialize in world-wide environmental risk solutions.

NOTES:

[1] Daniel C Esty & Michael E. Porter, Ranking National Environmental Regulation and Performance: A Leading Indicator of Future Competitiveness? http://www.isc.hbs.edu/GCR_20012002_Environment.pdf

[2] Charles McElwee, Environmental Law in China: Mitigating Risk And Ensuring Compliance, referenced in China Environmental Law, http://www.chinaenvironmentallaw.com/

[3] The sustainable development journey, iisd http://www.iisd.org/business/sd_journey.aspx

[4] The Bottom Line on Sustainability, Project Management Institute http://www.pmi.org/business-solutions/~/media/PDF/Business-Solutions/The%20Bottom%20Line%20on%20Sustainability_FINAL.ashx

[5] "OKI Strengthens Compilation Functionality of its COINServ®-COSMOS-R/R Chemical Substance Information System to Comply with Latest Industry-Standard Survey Formats"

[6] Balu Sharma, "Managing the Achilles Tendon of Environmental Compliance & Supplier Management," EE Times http://www.eetimes.com/design/smart-energy-design/4013563/Managing-the-Achilles-Tendon-of-Environmental-Compliance--151-Supplier-Management

[7] Green Winners, A.T. Kearney http://www.atkearney.com/documents/10192/6972076a-9cdc-4b20-bc3a-d2a4c43c9c21

[8] Charles McElwee, Environmental Law in China: Mitigating Risk And Ensuring Compliance, quoted iEnvironmental Law In China. THE Book, China Law Blog http://www.chinalawblog.com/2011/09/environmental_law_in_china_mitigating_risk_and_ensuring_compliance.html

[9] See for example "Yes, We Did: Canadian Mining Company Admits to Polluting U.S. River for Over 100 Years," Take Part http://www.takepart.com/article/2012/09/11/canadian-company-admits-it-has-been-polluting-american-river-over-100-years-0

[10] "REACH," http://ec.europa.eu/environment/chemicals/reach/reach_intro.htm

[11] Jonathan Hughes & Matt Whitteker, "Global Environmental Regulations: Implications for North American Business," Center for a Better Life http://www.centerforabetterlife.com/eng/magazine/article_detail.lasso?id=150

[12] Lower-volume companies presently are exempt, but eventually all companies conducting business in Europe will need to comply. See Amy Westervelt, "How International Regulations Are Changing American Supply Chains," Forbes http://www.forbes.com/sites/amy-westervelt/2012/05/10/how-international-regulations-are-changing-american-supply-chains/

[13] Tom Krawczyk & Bob Warren, International Challenges in Environmental Compliance and Supply Chain Sustainability http://www.conexant.com/company/docs/gsa_forum_conexant_article.pdf

[14] "How does Commerce define Sustainable Manufacturing?" U.S. Department of Commerce http://www.trade.gov/competitiveness/sustainablemanufacturing/how_doc_defines_SM.asp

[15] Green Winners, A.T. Kearney http://www.atkearney.com/documents/10192/6972076a-9cdc-4b20-bc3a-d2a4c43c9c21