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SUPERFUND REFORM ACT OF 1994

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BEFORE THE

COMMITTEE ON FINANCE
UNITED STATES SENATE

ONE HUNDRED THIRD CONGRESS

SECOND SESSION

ON

S. 1834

SEPTEMBER 14, 1994

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SUPERFUND REFORM ACT OF 1994

WEDNESDAY, SEPTEMBER 14, 1994

U.S. SENATE,
COMMITTEE ON FINANCE,
Washington, DC.

The hearing was convened, pursuant to notice, at 10:30 a.m., in room SD–215, Dirksen Senate Office Building, Hon. Daniel Patrick Moynihan, Chairman of the Committee, presiding.

Also present: Senators Baucus, Bradley, Rockefeller, Daschle, Breaux, Conrad, Packwood, Roth, Danforth, Durenberger, and Grassley.

OPENING STATEMENT OF HON. DANIEL PATRICK MOYNIHAN, A U.S. SENATOR FROM NEW YORK, CHAIRMAN OF THE COMMITTEE

The CHAIRMAN. A very good morning to our distinguished witnesses and our guests. We are convened this morning to consider the provisions of the Superfund Reform Act of 1994.

The legislation comes to us, as is obvious, late in the year, but not too late, we hope. We understand that last night a vastly complicated agreement was reached between enormously powerful and mysterious forces in America.

Secretary Munnell has offered——

Senator PACKWOOD. Are you talking about the New York primary? [Laughter.]

The CHAIRMAN. Secretary Munnell has offered to provide a tutorial for any member of the committee that requests, so that is a rather formidable proposition on its own.

There are two categories of Superfund revenue issues to be addressed. First, is the essentially non-controversial proposal to extend existing Superfund taxes, which go back in some cases to 1980, and the second is the new Environmental Insurance Resolution Trust Fund, or "EIRF," I am sorry to say. That is what we are going to do this morning.

Secretary SAMUELS. That is the best we could do, Mr. Chairman.

The CHAIRMAN. And, on that note, I am going to turn the microphone over to Senator Packwood.

Senator PACKWOOD. I have no opening statement, Mr. Chairman.

The CHAIRMAN. Senator Baucus, you will have a statement, I am sure.

OPENING STATEMENT OF HON. MAX BAUCUS, A U.S. SENATOR FROM MONTANA

Senator BAUCUS. Thank you, Mr. Chairman. I appreciate you holding this hearing because I think it is critical that the second half of Superfund be enacted this year along with the first half.

Mr. Chairman, as you have stated, today's hearing is primarily about taxes authorized by Title 9 of the Superfund bill. And, with your indulgence, I would like to briefly explain the program that these taxes would support.

Superfund is one of our most important environmental laws. I think we will recall that almost all of our environmental laws are relatively young. They were enacted in the 1970's. They are all about, the major environmental laws, roughly 20 years old.

Superfund is one of the most important. Unlike other environmental laws, however, it does not prevent pollution, rather, it cleans up pollution that occurred in the past.

Our Nation's industrial development resulted in many great accomplishments, but there was an unfortunate by-product. That is, thousands of contaminated sites were left behind from one end of the country to the other: chemical waste dumps in New Jersey, toxic mine tailings that dot the landscape of the mountain west, the residue of huge, Federal nuclear complexes at Rocky Flats, Colorado and Hanford, Washington. These sites pollute drinking water, they expose children to toxic chemicals, they destroy neighborhoods.

For example, in my State of Montana, toxic wastes were dumped into rivers and streams. They seeped into soils. In Mill Creek, high levels of arsenic found in children forced the evacuation of an entire town. In East Helena, the yards of almost 400 homes are being dug up because the soil is contaminated with lead. Similar examples exist in every State.

Superfund was our response. It embodies a commitment by the Federal Government to the American people, a commitment to repair that damage. This commitment is important and appropriate. We must reaffirm it.

At the same time, we must face facts. The program is not working well today. In fact, the program is a mess. States and local communities do not have enough say in decisions, clean-ups are too costly, too slow, and the Superfund generates wasteful litigation.

I was struck by an example in the Chairman's own State, the Ludlow landfill in New York. Two big companies faced Superfund liability so they sued 603 other parties. They literally went through the phone book to drag people into court: school districts, towns, small businesses, even the local donut shop and florist.

The Superfund Reform Act addresses these problems. It makes it easier for States to run the Superfund program, involves the people that live in the neighborhood where a site is located, and makes clean-ups quicker and cheaper, and it reduces litigation by reforming the liability system and establishing a settlement process for policyholders and insurance companies.

Overall, the bill will reduce clean-up costs by 20 percent, reduce the time that clean-ups take by 25 percent, and reduce transaction costs by 50 percent. The tax provisions are, for the most part, straightforward: extend the feedstock tax and the corporate envi-

ronmental tax. They also create a new tax to support the Environmental Insurance Resolution Fund.

Let me explain why this fund is important. One of the main reasons for high Superfund costs has been litigation between policyholders and insurers over whether insurance policies cover Superfund liability.

This litigation is complex and it is costly. More than 1,500 cases are pending in courts around the country and the litigation costs are about $800 million each year. The new fund will encourage policyholders and insurers to voluntarily settle their claims.

This, as Secretary Bentsen has said, will go "a long way toward removing the uncertainty of litigation from the picture and that allows us to save on the cost of settling coverage claims, and that money can be put to better use cleaning up communities instead of paying lawyers and consultants."

A key question is how we raise the revenue for this settlement process. I am pleased that we appear to be very close. In fact, the latest word is an agreement was reached last evening. I look forward to exploring details during today's hearing.

Before concluding, however, I would like to make one more brief point. As the end of the Congressional session draws near, members may be tempted to consider adding extraneous amendments to any tax bill that looks like it has a good chance of being enacted. I understand the temptation. In fact, I may have succumbed to it once or twice myself in my younger years.

But, if extraneous amendments are added here in the committee, many more, obviously, will be added on the floor and that will make it impossible for us to complete a conference with the House.

As a result, we would have squandered an opportunity to enact a landmark bill that will save money, reduce litigation, and protect public health. So I hope we will limit our amendments to those directly related to Superfund.

Thank you, Mr. Chairman.

The CHAIRMAN. Thank you, Senator Baucus.

And, as we have a long morning ahead and part of the afternoon, let us begin by welcoming our most distinguished associates from the Department of Treasury, Hon. Alicia Munnell, who is Assistant Secretary for Economic Policy, and our omnipresent friend, Leslie Samuels, who is Assistant Secretary for Tax Policy.

In deference to the pleasure, which is rare, of having you before us, Dr. Munnell, would you begin, please? You put your statement in the record and commence your tutorial.

STATEMENT OF HON. ALICIA H. MUNNELL, ASSISTANT SECRETARY FOR ECONOMIC POLICY, U.S. DEPARTMENT OF THE TREASURY, WASHINGTON, DC

Secretary MUNNELL. Thank you very much, Mr. Chairman. My initial intention was to give an overview of the need for reform and an overview of this bill. Senator Baucus has already very ably laid out the need for reform, so let me just briefly summarize why I think this bill is so important.

The wisest observation I have heard during this whole process, which has gone on for the past year and a half, is that if people facing Superfund liability thought that they were going to be allo-

cated their fair share of the costs, and if they thought that the money that they spent was going to be spent wisely, the litigation would end and the clean-up would begin.

The problem is, we have had unrealistic, Cadillac-type clean-up standards that require, in some instances, that children virtually be able to eat the dirt even if a factory is going to be built on the site. One very important part of this reform is we are going to put in sensible clean-up standards.

The other issue is liability, and there are two aspects of this. The first is figuring out how much contamination each potentially responsible party is responsible for, and this will be done by sitting people around the table and figuring out their fair share based on their volume and toxicity of their waste. This should eliminate all the litigation between PRPs—potentially responsible parties—that we see under the current system.

The second major area of litigation is between the PRPs and their insurers. Basically, what happens is after PRPs are identified by EPA and they are found liable for clean-up costs, the parties go to their insurers and say, we would like to collect from you.

The insurers say, we were not insuring you for that because it was prior to 1980, and, therefore, we do not want to pay. These disputes inevitably end up in the State courts. The resolution of these disputes varies immensely by State. It is capricious, and it is wasteful, and leads to slow-down of the entire process.

So, as Senator Baucus indicated, the EIRF title is an extremely important part of this entire bill. It establishes a fund so that when PRPs come away from the allocation table and they are assigned their share of the costs, they can go over to the EIRF window, present their bills, and, based on the offer from the EIRF, decide whether or not they want to accept this pay-out, which will vary depending on where their sites are located and where they have established litigation venue, or whether they want to go ahead and sue.

If their sites or venues are in States such as California where the courts have generally found for the PRPs, they will receive 60 cents on the dollar, if their sites are in States where the insurers tend to win, such as Florida, they will receive 20 cents on the dollar. Most States fall in the 40 cents on the dollar category.

If they accept the EIRF offer then they waive the right to sue. It is a once and for all option so that the PRPs cannot cherry-pick. And, if they decide not to accept, they have not lost any rights they have under the current system.

This plan originally started as a 5-year plan with $3.1 billion. It has been extended to an $8.1 billion plan over 10 years, with continued financing thereafter to pay off obligations incurred in the first 10 years.

So, in short, the Administration's Superfund reform proposal is a really valuable piece of legislation. It will reduce clean-up costs and it will reduce litigation costs. Businesses will save money and the sites will get cleaned up.

This is really important, not only because Superfund sites are health hazards, but also because they are economic hazards. These sites need to be cleaned up and redeveloped so that they can add—

not subtract—to the well-being of the communities in which they are located.

We have all spent an enormous amount of time and effort trying to reach appropriate compromises on difficult and delicate issues. The proposed bill makes great strides in addressing the many shortcomings of the current system. That is why the Administration is so happy to support it, and, even more important, why it has broad-based support from industry, from small businesses, from environmental groups, and from the insurers.

Thank you very much.

The CHAIRMAN. That certainly is a most auspicious beginning of a hearing. I mean, it is succinct and clear. Your testimony is important to us. If it is good enough for you, it must be pretty good.

[The prepared statement of Secretary Munnell appears in the appendix.]

The CHAIRMAN. Let us see if it is good enough for Mr. Samuels.

STATEMENT OF HON. LESLIE B. SAMUELS, ASSISTANT SECRETARY FOR TAX POLICY, U.S. DEPARTMENT OF THE TREASURY, WASHINGTON, DC

Secretary SAMUELS. Mr. Chairman and members of the committee, I would ask that my written statement be placed in the record.

The CHAIRMAN. Of course, sir.

[The prepared statement of Secretary Samuels appears in the appendix.]

Secretary SAMUELS. I am pleased to describe the Administration's proposals for funding the Superfund Reform Act, S. 1834, including, in particular, the Environmental Insurance Resolution Fund.

Before discussing the environmental insurance reform mechanism, I would like to briefly address the extension of certain existing taxes in connection with Superfund reform.

As you know, we now finance the Hazardous Substance Superfund Trust Fund with excise taxes on domestic crude oil and imported petroleum products, certain chemicals and imported derivative products, and a corporate environmental tax. These taxes are scheduled to expire at the end of 1995.

Under S. 1834, the Superfund Trust Fund has continuing financing needs. Consequently, these excise taxes and the corporate environmental tax would be extended to the end of the year 2000.

Now, I will turn to the topic of the financing of the Environmental Insurance Reform. The proposal that I will describe is the bill that was favorably reported by the House Committee on Ways and Means, with some modifications.

The modifications, which follow the approach of the Ways and Means bill, reflect extensive discussions that have taken place over the last few weeks.

First, I will describe the modified proposal, and I will conclude by highlighting the changes from the bill reported by the Ways and Means Committee.

The PRP insurance industry litigation involves whether insurance policies written prior to 1986 covered losses from environmental damage. Why before 1986? Because insurers changed their policy forms in 1986 to exclude environmental liability from cov-

erage. For pre-1986 insurance, the issue is whether the policies covered losses from environmental damage.

The fight over this issue goes on and on, and the parties have spent enormous sums of money. As a result of this litigation morass, only 12 cents of every dollar spent by the insurance industry has gone to cleaning up hazardous waste sites.

This extremely unfortunate situation which involves very real social and economic costs has driven all parties towards reform. As Secretary Munnell said, that is why the Administration has proposed the Environmental Insurance Resolution Fund, which I will refer to as the fund.

Reform through use of the fund goes a long way to remove the uncertainty of litigation. It allows everyone to save on the time and costs of settling coverage claims and to devote those resources to cleaning up sites.

The fund is a vehicle to facilitate settlements between PRPs and insurers. When the PRPs accept their settlement offers from the fund, the fund must have the financial resources to make good on those offers.

Under the Administration's original proposal, the fund would need $3.1 billion for the first 5 years of its life, so we designed a financing mechanism that would require the insurance industry to pay into the fund $3.1 billion over 5 years.

When the Senate Committee on Environment and Public Works favorably reported the legislation, the 5-year proposal became a 10-year proposal, so additional funding of $5 billion for five more years was needed.

To determine how to equitably raise the necessary funds, we have met with many insurance industry representatives to gain a better understanding of the Superfund problems and the issues arising from various proposals. In the context of these extensive and ongoing discussions, we have looked to three principles for guidance.

The first principle, is that those insurance companies that stand to potentially benefit the most from insurance litigation reform should bear a significant share of the funding. These are the insurers that are facing mounting problems today from Superfund liability claims.

The second principle, is that a broader segment of society will also benefit from the insurance reform effort. Policyholders will benefit from reduced litigation, the rest of the insurance industry will benefit if their brethren remain solvent, and society will benefit from the reduced cost of litigation and quicker clean-up of sites, so we believe that those who will benefit from reform should contribute to the funding.

The third principle, is that all commercial insurers and reinsurers, whether domestic or foreign, should participate in financing the fund because they all benefit from reform.

Given these three principles, we are proposing today what we believe is a reasonable financing approach for the fund, whose framework is supported by a significant segment of the commercial insurance industry.

Under the proposal, the financing of the fund would be split almost equally on a present value basis between retrospective and

prospective taxes. And I would refer you to page five of my written testimony. There is a table there that shows the dollar targets that this proposal has, and which I will now describe in, really, percentage terms.

During the fund's first 4 years, roughly 69 percent of the funding would come from separate retrospective taxes on insurers and reinsurers that wrote commercial coverage before 1986 from which Superfund claims could arise.

About 46 percent of the total tax would be raised from direct premiums, and about 23 percent would be raised from reinsurance premiums. Also during the first 4 years, approximately 31 percent of the funding would come from prospective taxes on direct insurers that write insurance in commercial lines of insurance after the date of enactment.

During years 5–10 of the fund, approximately 66 percent of the funding would come from the prospective tax on direct insurers that write insurance in commercial lines of business. A retrospective tax on reinsurance premiums would raise approximately 23 percent of the fund's revenues.

And I would like to note that we understand from the reinsurers that this 23 percentage target approximately reflects the total domestic and foreign reinsurance market share in the base period years.

The remaining 11 percent of the fund's financing would be contributed through an assessment on direct insurers that wrote insurance coverage that gave rise to actual Superfund claims for which the fund makes awards.

To provide the insurance industry with assurances that taxes collected would not exceed the revenue targets, the various taxes would trigger off when the necessary revenue is raised.

Each of the tax pools, whether prospective or retrospective, and whether on direct or reinsurance premiums, would be designed to trigger off once the appropriate revenues are raised within multi-year timeframes.

In addition, within the retrospective tax on reinsurance premiums from which 23 percent of the financing would be raised, the domestic and foreign reinsurers would have separate multi-year revenue caps and there would be one overall multi-year revenue cap at 23 percent of the fund's total revenue.

The fund could have continuing obligations beyond its anticipated 10-year term. Treasury would conduct a study in the 9th year of the fund to make recommendations with respect to the insurance industry's financing of the fund after the tenth year.

Absent Congressional action, the funding provided for in the proposal would continue until ongoing obligations of the fund are satisfied.

The retrospective taxes I have just described are consistent with our first principle, that those insurers that could benefit most from reform should pay for a significant share of reform. These taxes will be paid in the future. They replace an existing, but uncertain, liability arising from insurance coverage that an insurer or reinsurer wrote in the past.

Our proposal uses historic premiums as a proxy for potential liability. We believe that the premium proxy, with its $50 million de-

ductible for direct writers of insurance represents a reasonable connection between an insurer and potential Superfund liability.

Upon payment of these retrospective taxes and with the rest of the reform package, insurers and reinsurers that wrote significant commercial business from 1968 through 1985 would be relieved of uncertainty with respect to both the amount and timing of litigation costs and liability.

As another element of the retrospective proposal, each direct insurer would be assessed by the fund each time the fund makes an award that relates to a policy that the insurer wrote in prior years. These assessments begin in year five and would raise annually approximately 11 percent of the financing of the fund from direct writers.

Our proposal also contains a prospective tax. Approximately 50 percent of the financing—31 percent in years 1-4, and 66 percent in years 6-10—would be paid by insurers writing new insurance in commercial lines. More lines are included than in the retrospective tax base in order to preserve the stability and predictability of the revenue base.

Since Ways and Means reported out its bill, we have had discussions with various parties about the lines of businesses included in the tax base. Based on those discussions, we would recommend that the committee provide exclusions for insurance coverage in the financial guaranty and fidelity lines of business.

In addition, we had not intended to include personal insurance coverages, such as insurance of private, owner-occupied residences and personal liability umbrella policies in the tax base, and would recommend that the committee exclude such personal coverages.

Each year, with respect to the prospective tax, the first $5 million of covered premiums written by an insurer would be exempt from the tax. This helps ease the burden on all insurers and takes many small insurers completely out of the tax.

We anticipate that, over time, insurers would certainly try to pass this prospective tax through to policyholders as a cost of doing business. Thus, this portion of the funding would be spread broadly among insurers, their policyholders, and society. However, we understand that, as a result of market forces, it is unlikely that this prospective tax would be passed through by insurers to reinsurers.

Now, I would like to briefly describe how alien insurers participate in the financing proposal. With respect to the retrospective portion of the funding, an alien insurer would be subject to a tax of one-half of 1 percent, based on the amount of risk it assumes under each casualty insurance contract it writes. It is a tax imposed on an insurer's——

The CHAIRMAN. Mr. Secretary.

Secretary SAMUELS. Yes.

The CHAIRMAN. A query has made its way around the committee here. An alien insurer?

Secretary SAMUELS. Yes. There are foreign insurers, some of whom are engaged in business in the United States, and there are other foreign insurers who are not engaged in a trade or business in the United States.

The foreign insurers that are engaged in a trade or business, because they are here and they have a physical presence, are in-

cluded in the retrospective tax base just like a domestic insurance company.

The CHAIRMAN. And the others are aliens.

Secretary SAMUELS. The others are aliens because we do not have any——

Senator BRADLEY. Well, we could call them the green card insurers.

The CHAIRMAN. The green card insurers.

Senator BAUCUS. No, the first to green card.

Senator BRADLEY. First to green card.

The CHAIRMAN. Are these illegal aliens? These are legal aliens. [Laughter.]

Sorry. We have just got to get this record straight.

Secretary SAMUELS. These insurers, the foreign insurers that are not engaged in a trade or business, are subject to a one-half of 1 percent tax based on the amount of risk assumed under each casualty insurance contract it writes.

And, as I say, this is a tax imposed on assumed risk rather than the premium paid. To avoid paying this tax on all casualty contracts written, the alien insurer could elect to pay the same retrospective tax that I described earlier, so they can elect to be treated exactly like everyone else, all of those foreign insurers that are doing business here, and the domestic companies that are subject to the retrospective tax.

The alien insurer would make a preliminary election to pay the retrospective tax, post adequate security with the Treasury, and then execute a closing agreement with the IRS under which it would agree to pay the proper amount of retrospective tax.

With respect to the prospective tax, alien insurers would pay the same prospective tax as all domestic and foreign insurers. They are all exactly on the same footing.

Now, I would like to highlight, briefly, the changes from the bill reported by Ways and Means. These changes are described in somewhat more detail on pages 14 and 15 of my written testimony.

First, the revenue targets have been modified slightly. The total has not changed; it remains $810 million per year. We are targeting $8.1 billion over 10 years; that is $810 million a year. We have not at all modified that target. However, the retrospective tax target for reinsurance has been reduced by $12 million to $188 million.

The $50 million exclusion from the retrospective tax base will be allocated entirely to direct insurance premiums rather than allocated proportionately between direct and reinsurance premiums. This means that the $50 million exclusion would not apply to reinsurance.

Next, the reinsurers would participate in the financing through a retrospective tax rather than a combination of taxes and assessments. The reinsurers had requested to be subject to assessments and the retrospective tax, but they have reconsidered that due to the complexity of the assessment process for them.

We have also added, as I have described, multi-year caps which would trigger off the various taxes to avoid over-collections and special multi-year caps would be provided for domestic and foreign

reinsurers with respect to the retrospective tax on reinsurance premiums.

Next, absent Congressional action, the taxes and assessments would continue to finance any continuing obligations of the fund beyond its anticipated 10-year term, and, finally, the prospective tax base would be modified to exclude personal insurance coverages, as well as financial guaranty and fidelity insurance.

There has been considerable discussion and controversy within the insurance industry about how the financing package should be structured. We believe that the revised proposal represents a reasonable compromise and follows the Ways and Means bill.

In this regard, insurers and reinsurers that write approximately 60 percent of the fund's taxable premiums support the framework I have described to finance the fund.

Understandably, the supporters of the framework continue to be interested and concerned about: 1) the caps applicable to the reinsurer's retrospective tax, and 2) the tax rates which will be revised to generate the revenue targets I described and to reflect the modifications to the tax base and new information that has recently become available.

We hope that the insurers' and reinsurers' concerns will be addressed in the coming days. And I would note that, of course, the caps that we have proposed on the various tax pools should relieve some of the pressure on the tax rates for the insurers and reinsurers.

I want to emphasize that the Administration is wholeheartedly supportive of the need for Superfund reform. We believe that this financing proposal constitutes the missing piece necessary to complete the Superfund reform puzzle.

Mr. Chairman, this concludes my statement. Secretary Munnell and I will be pleased to answer any questions you and members of the committee may have.

The CHAIRMAN. We thank you, Mr. Secretary.

May I note that a quorum is present? And, as we will have nominations for Treasury officials at the end of the day, I am going to, with Mr. Packwood's agreement, we will say, a rolling quorum having been established, we can proceed with those.

Just one quick question. Did you indicate there are agreements still to be concluded in coming days?

Secretary SAMUELS. Mr. Chairman, this has all been carefully written. I want to get the exact words. The insurers and reinsurers that write approximately 60 percent of the fund's taxable premiums support the framework that I have described.

Understandably, the supporters continue to be interested and concerned about the caps applicable to the reinsurance retrospective tax and the tax rates, which will have to be revised. And, subject to their satisfaction on those numbers and how we are going to arrive at them, they have told us they support this proposal.

The CHAIRMAN. So what we have before us is a final, there is nothing to come?

Secretary SAMUELS. Correct.

The CHAIRMAN. Fine. Fine.

May I say, I was unintentionally discourteous to Senator Breaux, who was here at the outset of the hearings, and we did not give him a chance to make an opening statement if he wished to do so.

Senator BREAUX. I will just make an amendment in lieu of an opening statement.

The CHAIRMAN. You have an amendment?

Senator GRASSLEY. Mr. Chairman, could I make an opening statement?

The CHAIRMAN. Yes, you may.

Senator GRASSLEY. I came late.

The CHAIRMAN. Being mindful of a long morning ahead.

OPENING STATEMENT OF HON. CHARLES E. GRASSLEY, A U.S. SENATOR FROM IOWA

Senator GRASSLEY. Well, if I take more than three minutes just cut me off, because that is all I wanted to take.

Up until recently, if you followed what has been going on in this debate around the country, in particular regarding the Environmental Insurance Resolution Fund part of this bill, and if you followed it through the press, I think we would have been led to believe that a consensus was forming and that nearly the entire industry was close to getting on board for this Administration proposal.

I think things are obviously more complicated and uncertain than that. In fact, we know now that factions of the insurance industry that have around 50 percent of the market are opposed to this proposed new tax.

These, of course, may be the so called "small insurers," but they are more important to the small and rural areas than, perhaps, the large insurers that have come to an agreement.

So, in the real world—and I know that it is difficult to be in the real world in this town—we are still a long ways from a consensus. It seems to me that in the few weeks that we have left in this session there is going to have to be a lot more of a consensus than exists now before this proposal gets very far.

So my feelings at this point are that this new tax proposal remains very controversial and there is a lot more work that is going to have to be done. We all want to clean up the environment, and there is probably a great deal of support for the underlying Superfund Reform bill. We want to provide help and incentives for the private sector to do its part, but it needs to be a fair burden, and it does not look like we are there yet.

Thank you.

The CHAIRMAN. Thank you, sir.

Let me then just say, is there any other Senator who wishes to make an opening statement as against addressing queries to our witnesses?

[No response.]

The CHAIRMAN. I assume otherwise.

Senator Packwood?

Senator PACKWOOD. I have no questions, Mr. Chairman.

The CHAIRMAN. Then I will ask one question, if I may. And, conscious of the presence of Senator Danforth as a sometime State At-

torney General, you break down the States into three categories based on the pattern of jury awards in litigation.

And I am not surprised that juries are very narrow in their sympathies in Maine, that being a category that we well understand, but also in New York. In New York you will only get 20 percent from this fund when you apply.

On the other hand, those great-hearted folk in New Jersey, you get 60 percent from them, as in West Virginia, where obviously the juries have larger sympathies with their fellow men. But we are mainstream.

Senator BAUCUS. We are mainstream.

The CHAIRMAN. Can I just ask, what is the statistical basis for this, is this one standard deviation? Alicia, we need a tutorial.

Secretary MUNNELL. This was not a classification that was done by the Administration, this was a classification that was done by industry and insurers, and this is their assessment on how PRPs and insurers have fared in the different States.

The notion was that the percentages should reflect, as closely as possible, the outcome of litigation, and maybe even add a premium to induce people to come in and settle with the fund. So this is the result of negotiations between the parties directly.

The CHAIRMAN. But I want to make the point, and we can get back to it, what is the data base? Has the Department of Commerce, the Bureau of Census, the Bureau of Labor Statistics gathered data or did the percentages result from the impressions of the people with whom you have had good faith negotiations?

Secretary MUNNELL. There are no real experts on this area in the country. There is no good, solid data to underline it. But the people involved have had vast experience in this area and the two parties brought the information to the table, and this was a mutually agreeable settlement between the insurers and the PRPs.

The CHAIRMAN. But you would grant that it has a touch of the anecdotal about it.

Secretary MUNNELL. This whole EIRF is the product of a negotiation.

Senator BRADLEY. Mr. Chairman.

The CHAIRMAN. Senator Bradley, on behalf of the great-hearted folk of New Jersey.

Senator BRADLEY. Well, I guess it is troubling that we would be contemplating any legislation that would, in any way, be based on the anecdotal.

The CHAIRMAN. That is right. We have never done that before.

Senator BRADLEY. I think that it should always be hard data, in the absence of which, of course, anecdotal has to suffice. And I do not know the answer to your question. I think it is a legitimate question.

Might one hypothesize that in States where there are more actions, and where there are more sites, and where there is a more active bar in this area, you might find that there are higher numbers? It seems to me that that is——

The CHAIRMAN. That should also suggest that State laws are different as well.

Secretary MUNNELL. Right. These are not to reflect jury awards, they are more to reflect State laws as applied by the courts.

Senator BRADLEY. Yes. And I might say that, at least in New Jersey, the issue of toxic waste dumps was addressed first in the mid-1970's, and this was before we had a Federal Superfund law.

By the time we got a Federal Superfund law we had already charted over 1,200 toxic waste dumps, so we had a very active bar with regard to the State law and, therefore, a Federal law.

The CHAIRMAN. Thank you, Senator Bradley.

Senator Baucus?

Senator BAUCUS. Thank you, Mr. Chairman.

Secretary Samuels, one of the questions that has arisen, which was somewhat alluded to by the Senator from Iowa, is that this proposal applies the retrospective and also the prospective taxes to a very broad base of commercial insurance premiums, and it is quite possible, say, for a new insurance company or an insurance company that has been around for several years but did not write any policies that covered Superfund liability, to now complain that, gee, why should the tax be on me?

I did not write any policies that covered these eventualities in the past, or I am a new company, therefore, it is obvious my policies do not cover it, so I am precluding it, Superfund liability in my coverage. What is the Administration's response to those concerns?

Secretary SAMUELS. Senator Baucus, we have taken those concerns into account in formulating this proposal, and I would make the following points. First, this extensive litigation that we are talking about is a problem for the whole industry, not just a problem for the companies who wrote these policies going back before 1986.

And the reason it is a problem for the whole industry is that if the insurers that are being subject to these lawsuits have financial difficulties, for example, let us say some of them become insolvent, States have guaranty funds which are meant to support the insurance industry in the State. And those guaranty funds are financed by assessments on all the insurance companies in the State, whether they were in existence before 1986 or not.

So we view this as a problem for the entire industry. When we designed our proposal, as you can see, we have tried to balance retrospective taxes and prospective taxes to come out with what we view is a reasonable proposal.

In addition to that, with respect to this question about the smaller insurance companies, we have taken several steps to alleviate the burden of the financing proposal on them.

First, with respect to the retrospective tax, there is a $50 million exemption for direct writers of premiums during the retrospective period. The purpose of that was, in part, to reduce administrative complexity, but also to deal with small insurers.

With respect to the prospective tax, we have a $5 million exclusion per year so that you do not pay any tax on your first $5 million of premiums. That $5 million exclusion was designed specifically to deal with smaller insurers.

One of the things about this discussion, at least in my experience so far, is that you will hear a lot of points of view, and there are a lot of points of view and you will hear a lot of input.

And I think when you evaluate that information I would ask that people focus, when various interested parties come forward and say

that this tax is a problem for them, and I think the first question is, well, are you going to be subject to the tax, because we have the $5 million exclusion from premiums subject to the prospective tax; a $5 million per year exclusion. And, in addition to that, we have excluded personal lines, for example. The prospective tax only deals with commercial lines. So we have excluded a lot of the lines that small insurers write.

One of the small insurance trade associations has told us that our exemptions exempt 800 of their 1,250 members. Well, I think that goes a long way toward addressing their concerns.

Senator BAUCUS. Is there any precedent in the code, though, for a situation similar to the EIRF, that is, where a tax is imposed on a fairly broad cross-section of taxpayers, but the revenue collected is earmarked to a more specific, limited application?

Secretary SAMUELS. Well, the Superfund excise taxes and environmental——

Senator BAUCUS. Could you explain why that is precedent?

Secretary SAMUELS. That is one precedent where you have a reasonably broad-based tax to finance, in effect, the orphan sites that the Superfund pays for. It could not attribute, with respect to the orphan sites, the financing cost to the polluters who created the problem, since they have disappeared. So there is a relatively broad-based——

Senator BAUCUS. So you are saying the broad-based feedstock tax is an example.

Secretary SAMUELS. Right. Right. The other thing I would mention with respect to similarities between the basic Superfund tax and the corporate environmental tax that we have in this proposal is that those taxes trigger off after you have hit certain revenue targets.

Senator BAUCUS. You are talking about the reinsurance?

Secretary SAMUELS. Yes. Well, actually, we have the taxes triggering off after they hit the revenue targets for each category, including reinsurance, but also, on the prospective tax, the tax would trigger off when it hits its revenue target.

So we have borrowed that aspect, the triggering off aspect, to help the insurance companies who are concerned that the rates will be set at a level that will over-collect the target.

Senator BAUCUS. Right.

Secretary SAMUELS. So we have put these targets in. That was one of the changes from the Ways and Means bill that we have put in which we think is consistent with the approach that we have been following.

Senator BAUCUS. Thank you.

The CHAIRMAN. Thank you, Senator Baucus.

Senator PACKWOOD. Could I ask one question, if I might?

The CHAIRMAN. Yes, of course.

Senator PACKWOOD. Refresh my memory. It was not your Administration—I am not sure it was any Administration, and Senator Rockefeller would know—but what did we try to do with the coal companies and the UMW, did we try to impose a tax on coal companies that had no connection with that, and did we do it?

Senator ROCKEFELLER. No.

Senator PACKWOOD. Did we try to do it?

Senator ROCKEFELLER. That had been the original suggestion, and then it was not acceptable to the previous Administration because it was a tax and, therefore, we had to go to another——

Senator PACKWOOD. A tax on companies that had no connection with the UMW, with the contract, or any of the obligations.

Senator ROCKEFELLER. Right.

Senator PACKWOOD. All right.

The CHAIRMAN. Senator Durenberger.

Senator DURENBERGER. Secretary Samuels, you went back and looked at your comments just a bit earlier in today's statement. Would you go back and read the first part of your statement where you laid out the three principles and read the first principle to me so that I can understand that first principle a little bit better?

Secretary SAMUELS. Absolutely. The first principle is that those insurance companies that stand to potentially benefit the most from insurance litigation reform should bear a significant share of the funding. These are the insurers that are facing mounting problems today.

Senator DURENBERGER. That is fine. I am going to read from testimony that will come later—and I may not be here for that—from a gentlemen from, I think, Reliance, speaking on behalf of the National Association of Independent Insurers.

This is a quotation from your testimony, July 25, 1994, before the House Ways and Means Committee with regard to that very same principle, and I, first, want to get the principle, then I want to ask some questions, if I still have time, about its given effect.

Here is the way his statement quotes you before the Ways and Means Committee. The first principle is "insurers that benefit from the Environmental Insurance Resolution Reform, those that have potential Superfund liabilities through commercial insurance coverage written in the past, should provide most of the EIRF's funding."

Most, as opposed to a significant share. If that is an accurate assessment of your statement, how do the words, "a significant share," differ from the word, "most," in a statement of principle?

Secretary SAMUELS. Senator Durenberger, we made a proposal originally that had a split between retrospective and prospective on a 70/30 basis. That was the original proposal that we made, and we thought that that was a reasonable proposal and it was particularly a proposal to start the discussions. I think everybody who has been involved in this process knows that this is only going to work when we get a significant part of the industry to agree.

Senator DURENBERGER. Are you still at 70/30?

Secretary SAMUELS. No, we are at, on a discounted basis—and this is the Ways and Means bill—of approximately 50/50. It obviously depends on what discount rate you use, but, on the discount rate we are using, which I believe is a Treasury rate, the retrospective tax is just over 50 percent.

So we are, in our minds, about there and the reason that we changed the word from "most" in the Ways and Means Committee to this is that we are just over 50 percent. I do not view the difference between above 50 or just below 50 as really significant for this purpose.

Senator DURENBERGER. Yes.

Secretary SAMUELS. But, in order to be precise in our testimony, that is the reason why we changed it.

Senator DURENBERGER. All right. But you still call it a principle, even though the word "most" is now the word significant and you admit that it is practically a 50–50 deal.

Secretary SAMUELS. Correct.

Senator DURENBERGER. I, frankly, do not see that that is a principle anymore, but I do understand where you are coming from.

Secondly, and these are just factual questions because I have not been part of the negotiation, in that very same statement by Howard Steinberg he says, "The resulting proposal does not represent a compromise widely supported in the property and casualty industry.

"To the contrary, it is opposed by the overwhelming majority of P&C insurers as representing an attempt by a few large, primarily east coast insurance companies to shift their environmental liability to the rest of the industry."

Then he goes on to explain how this came about and who the folks in the P&C insurance and reinsurance industry are part of this deal, and alleges that the vast majority are not part of it. Is that factual?

Secretary SAMUELS. Senator Durenberger, I have not seen the statement. You will have to realize that I have not read the words, but I would make the following observations.

When you hear statements about this issue from various interested parties, first, you should ask people whether they, in counting numbers, are subject to the tax. It does not seem to us that if you are exempt from the tax you should really be concerned about the proposal. If you are not in the tax base and not subject to the tax, it does not seem to us—

I mean, we, of course, want comments from everybody, but for companies that are not subject to the tax, it seems to me, their voice ought not to carry very much weight at all.

Second, we do not think counting numbers of companies of those who are subject to the tax is appropriate either, we should look at market share and look at the total premiums and the premiums that are subject to tax. Insurers that are responsible for premiums subject to tax that support this framework——

Senator DURENBERGER. Mr. Chairman?

The CHAIRMAN. Please.

Secretary SAMUELS. —are about 60 percent of those premiums.

Senator DURENBERGER. Great. I appreciate the response. I just want to say to the Chair and my colleagues that I do not have time to ask other questions now, and if I am not here at 12:00 o'clock because of another commitment to ask Mr. Steinberg, I would ask him to define it. The only reason I am doing this is, there is also a substantial expansion of the definition of the commercial insurer.

The little we know about how the insurance industry operates means that a lot of people who are not, in America, in the future, in particular, and some retrospectively, were not selling insurance for Superfund liability purposes will end up carrying this. They will carry it on their homeowners, they are going to carry it on a lot of things, which is why I raised the question.

Secretary SAMUELS. Senator Durenberger, let me—may I just interrupt you for one minute?

The CHAIRMAN. Yes. Please. Please.

Secretary SAMUELS. I am sorry. But homeowner policies will not be subject to this tax base.

Senator DURENBERGER. All right.

Secretary SAMUELS. We have taken out personal lines. And I think that that testimony was prepared before they have heard our testimony today. And in our testimony today——

The CHAIRMAN. Well, we will have the chance to ask Mr. Steinberg, if you want to leave questions behind for us to him.

Senator DURENBERGER. I just want to say, because there is such a big turnout here, and all that sort of stuff, and I know there is a lot of money at stake, just so you understand where I am coming from in my experience here, the last time we did a bill similar to this when we were trying to do tax policy on insurance companies, I think we acknowledged here in the Finance Committee we are not experts on the insurance industry and we had this debate between the stocks and the mutuals and we left it to them to resolve the debate——

The CHAIRMAN. We did.

Senator DURENBERGER [continuing]. And decide what we ought to do, and then, in fact, we endorsed it. And, as I read through all of this testimony and I follow the history of this, I find that a lot of us are being put in that kind of a position, that if we accept the notion that this has nothing to do with Superfund, really, this has everything to do with contracts made in the past between insurers and insurance and the way in which the evolution of time, and fact, and circumstance impacts on those contracts.

We now have those contractors coming in and saying, we will not be able to fulfill the obligations of our contract, we have fought fulfilling them since 1985, as a matter of fact, and we now want you to help us resolve this problem and we want the rest of the industry to help us resolve this problem, and here is what we in the industry have concluded in some kind of an agreement or a comprise, and then they hand it to us and say, this is the best we can do.

And that is why I asked the question about, if it is a principle, that is one thing. If it is overwhelming by whatever numbers, that is something else. I kind of have to understand whose part of the deal and what the rest of this deal is.

And I suspect there are others around here who had some experience with this particular industry in the past, whether it is over tax policy or something else, who will be asking those same questions.

Thank you, Mr. Chairman.

The CHAIRMAN. Senator Grassley, you are next.

Senator GRASSLEY. Thank you, Mr. Chairman.

Senator Baucus, would you listen while I ask a question that follows up on what you asked?

Senator BAUCUS. I am right here.

The CHAIRMAN. Senator Baucus, you listen. The Chair rules that Senator Baucus will listen. [Laughter.]

Senator GRASSLEY. I want to get back to the State guaranty fund argument that was put forth. And I imagine the first question you

will have to speculate on, so do not spend a lot of time on it, if you have to.

Do we have any evidence that these insolvencies will occur? But, most importantly, I want some sort of reaction from you or rebuttal to an argument that some in the insurance industry would give, that maybe some of these companies would rather take their chances with propping up these State guaranty funds because at least, if they were in that position, they would benefit from getting increased business from those companies who lose clients because of the insolvencies. At least they would have some revenue there to pay it, increased business.

Secretary SAMUELS. Senator Grassley, I would respond to you in the following way. This litigation morass is a problem for, in our view, the entire industry. With respect to the companies that wrote policies prior to 1986 that are the subject of these costly and lengthy lawsuits, if you look at the credit ratings and how the financial markets are kind of looking at these companies, you can tell that there is a problem. I think that is what is pushing people to try to solve this problem. So I cannot tell you that a particular company or group of companies might become insolvent; I do not think anybody can do that.

What we do know, is that there is an enormous amount of uncertainty in this area, uncertainty as to timing of liability and an uncertainty of amount, and that is hurting the insurance industry and the companies.

Senator GRASSLEY. Well, then what about those companies that want to——

Secretary SAMUELS. Now, with respect to the companies that I guess subscribe to the Darwinian principle that the fittest will survive, I guess it seems to us, from a public policy point of view, that to say that we see this problem——

And, by the way, the sites are not being cleaned up. I mean, let us look at what the big picture is. The sites are not being cleaned up.

If the idea is, for those companies who think that they might beat the system, to say, well, do not do anything, we will just watch this train wreck occurring, we will watch the next train come along and crash, and the one after that. For those people I would say that I do not think, as a policy matter, we should just watch this thing happen and allow insurance companies to go into insolvency.

You will remember, with these guaranty funds, anytime you have that situation it hurts not just the shareholders, it hurts the policyholders, and there is an enormous cost in dealing with insolvent companies.

So this is an issue that we think needs to be addressed and we think that there is a lot of uncertainty and the type of proposal that we are talking about is a very reasonable proposal.

Senator GRASSLEY. I do not know whether there is a lot of Darwinianism in our market. There is a predictability in the marketplace that I think these people are willing to accept, and there may be a train wreck, in your opinion, down the road, but there is still an alternative that they see here, and they see that as a

more predictable alternative than what we might be presenting them.

Let me move on. The Ways and Means bill appears to grant the Treasury Department authority to designate additional lines of business to be subject to the prospective tax. Does the proposal before us include this authority, and, if so, is it limited to commercial lines?

Secretary SAMUELS. Senator Grassley, the proposal that you have before you does contain that authority, and that authority is limited. If you look on page 14 of our written testimony where we describe some differences between the Ways and Means bill and the proposal that we have brought to the committee today, Number 3 says, "The Secretary of the Treasury's authority to extend the prospective lines of coverage other than those originally identified as covered lines would be clarified to provide that such authority is intended to allow the Secretary to respond to changes in the construction of the annual statement lines and does not extend to reinsurance."

What we are worried about is people gaming the system, or somebody creates a new line that really is a substitute for an old line. So the authority, in our view, is really quite limited.

The CHAIRMAN. Thank you, Senator Grassley.

Senator Breaux?

Senator BAUCUS. Mr. Chairman, might I just tell the Senator.

The CHAIRMAN. Yes.

Senator BAUCUS. I listened to him and I listened to Secretary Samuels. I think he made some good points, but I just think that the Secretary is right, this is a broad societal problem we have. A lot of clean-ups will not take place if you do not take some action similar to what is suggested here.

I just think it is a little self-serving for companies to say, do not solve a big problem because we want to be around to pick up some of the pieces that are left over and get their business. That is a little, I think, of what is happening here. But I wanted to tell the Senator I did listen to him, and I thank him for drawing this to my attention.

Senator GRASSLEY. Mr. Chairman, in a very narrow area, is this commercial line that is going to be taxed applied to churches? I do not think churches are businesses. At least, not the churches I go to. Are they going to be taxed as a commercial line of business, churches?

Secretary SAMUELS. As I understand the proposal, the insurance on non-profit organizations is in a commercial line. What is excluded from our proposal is personal lines.

Senator GRASSLEY. Then churches are not going to be taxed.

Secretary SAMUELS. No, premiums for property and liability insurance covering churches is in the base. They are in the commercial line base.

Senator GRASSLEY. Then churches will be taxed.

Secretary SAMUELS. Correct. Commercial premiums are taxed. What is not taxed are personal lines, like personal liability umbrella policies or owner-occupied housing. That is excluded.

The CHAIRMAN. Thank you.

Senator Breaux?

Senator BREAUX. Thank you, Mr. Chairman.

I would just say, I have been waiting for 2 years for a tax bill. I never thought we would get one so complicated, though. I thought we would have something nice and simple.

I want to commend the Chairman of the Environment and Public Works Committee for bringing this legislation out of the Environment Committee. I was in the House in 1976 when we wrote RCRRA, the Resource Conservation Recovery Act. We thought we had helped solve the problem of hazardous waste then. Then we had to come back in 1980 with CERCLA and thought we had solved the clean-up problem.

And here we are in 1994 and we have realized that only a very small fraction of the Superfund money has actually been used to clean up, and we have been working on this since 1976. You talk about an example of government not working very well, this has got to be it.

With regard to the changes that the committee has brought forward, I think that they really are significant and go a long ways to resolving a problem that we have not resolved for 15 years, almost 20, now. So I think the Chairman and the members are to be commended for the product that is before the committee.

But I will tell you, I am trying to understand this tax. This has got to be the most complicated thing for a non-tax attorney that I have ever taken a look at, and I am sure there is a reason for it being so complicated in order to make sure it is fair.

Can you explain to me again, Mr. Secretary, what is the rationale for taxing insurance companies that have never written Superfund insurance policies in the past or are not writing such policies at the present time in order to get them to make a contribution to the EIRF fund?

Secretary SAMUELS. Senator Breaux, one principle that we described was that this Superfund litigation, the PRP litigation situation, is a problem for the industry and it is a problem for society. As you said, only 12 cents on the dollar that the insurance industry is spending is being used to actually clean up sites, and sites are not being cleaned up. I mean, that is a very serious problem for society.

Senator BREAUX. Well, why should not all of society pay for it then?

Secretary SAMUELS. Well, we think that the prospective tax that is going to be imposed on new, direct insurance written after the date of enactment will, to some extent, and possibly to a great extent, be passed through to the insureds and not necessarily be a direct burden on the insurance companies themselves.

And I would remind you that States, I think every State that is represented here, has a State insurance premium tax. And that tax, on the average, is about 2 percent of the premium, which is much greater than the premium that we are talking about. And the industry seems to deal with that, and we believe that that tax is passed on ultimately to the insureds.

Senator BREAUX. But those taxes are not used for purposes that the companies did not write the insurance for.

Secretary SAMUELS. Well, they are used for whatever the States decide they want to do. But if the industry as a whole right now

is being hurt by this situation, the uncertainty surrounding this hurts all companies—and I would even venture to say that some companies who have not had claims against them does not mean they are never going to have claims, assuming they have written——

Senator BREAUX. They will not have claims against them if they did not write a Superfund policy.

Secretary SAMUELS. Well, if they are brand-new companies, they would not, but if they were in existence before, they would.

Senator BREAUX. Take one of the companies that had never written a Superfund policy in their entire existence. Would they not be paying the tax for something they have nothing to do with?

Secretary SAMUELS. Let me just make one important comment, and I am sure you will hear this from the insurance companies later. No one thought that they wrote a Superfund policy. The policies were written before 1986, but they did not think they insured Superfund claims.

Now, the State laws have been applied, and that is why there is this difference between States. Some States have gone back and asserted liability. I mean, if you talk to the companies, they think that they did not write Superfund polices. They have been caught up, from their position, in an unfair situation because they did not think that they had covered this risk.

And, when you talk to those people, they are the ones who said at the beginning of the debate, that there should be no retrospective tax; the entire tax should be prospective. And, in fact, one of the small associations of insurers that Senator Durenberger mentioned, in the discussions——

The CHAIRMAN. Did you mean small association or association of small?

Secretary SAMUELS. Association of small insurers. Thank you. Suggests to us that there should be no premium tax whatsoever, and that their proposal was that we put a surtax on the corporate environmental income tax for insurance companies. They wanted a completely broad-based tax on insurance companies that was a surcharge on the environmental income tax. That was my recollection.

So I think that there has been a lot of ideas here, from purely retrospective taxes, to purely prospective taxes, to broad-based taxes. And I think what we have been trying to do is to shepherd the industry, or a significant part of the industry, to an agreement which we think is a reasonable agreement, taking into account these competing concerns.

Senator BREAUX. My concern is that we are taxing premiums, that are being paid by commercial automobile liability insurance, ocean/marine insurance, that really have nothing to do with Superfund. That is right, is it not?

Secretary SAMUELS. In terms of the base for the prospective tax, we think that it is very important to have a tax base that produces a predictable and sustainable level of tax.

Senator BREAUX. The answer, though, is yes?

Secretary SAMUELS. Also, those companies are going to be subject to the problems collaterally.

Senator BREAUX. I do not want justification, I am just trying to get the answer. The answer is, yes.

Secretary SAMUELS. I think that——

Senator BREAUX. Let me ask you a specific question. Is there going to be a premium tax prospectively on companies that write commercial automobile liability insurance?

Secretary SAMUELS. Policies that cover commercial fleets, yes, will be subject to the tax.

Senator BREAUX. How about for ocean/marine insurance?

Secretary SAMUELS. Yes. And I would suspect, if we talk to the insurers and talked about risks, they might explain to us that the fueling stations for these commercial fleets or the ocean-going ships have caused pollution and problems that have to be cleaned up.

Senator BREAUX. Are there any Superfund sites in the ocean?

Secretary SAMUELS. No, just in the ports.

Senator BREAUX. Are there any ports that have a Superfund——

Secretary SAMUELS. I do not know. But I am just saying——

Secretary MUNNELL. Yes.

Senator BREAUX. Yes. A Superfund site at a port?

Secretary MUNNELL. New Bedford.

Senator BREAUX. How about commercial fire insurance, would premiums on commercial fire insurance——

Secretary SAMUELS. Commercial fire insurance covers factories that might be associated with a site.

Senator BREAUX. Thank you, Mr. Chairman.

The CHAIRMAN. Thank you, Senator Breaux.

Senator Rockefeller?

Senator ROCKEFELLER. Thank you, Mr. Chairman.

As you indicated, Secretary Samuels, West Virginia, like a lot of other States, has a guaranty fund. And my understanding is that if one of the companies goes bankrupt, that others come in and contribute and pick up the claims of the former company.

Now, that, of course, is a very good thing for consumers, and it is also very good for companies that can afford to do that. I know this carries a little bit further from what John was saying, but, as a general matter, Darwinism is good for larger companies who can compete for business, but not so good for others.

So take something like a county mutual, for example, a small insurance company, and they only write rural fire insurance, something of that sort; what happens with those folks? They have got to pay into it, as I understand it. But they are small, and the company goes bankrupt. You have got a guaranty fund.

The current system is clear about what has to happen. Under the current system, is it the case that those small insurance companies cannot go out and get new business when other insurers fail?

Secretary SAMUELS. Senator Rockefeller, with respect to the operation of State guaranty funds, it is a State by State project and I do not know the details of them. But, as I understand the general principles, if you have a State guaranty fund it is there to backstop companies that become insolvent, and then that fund is financed by assessment on solvent companies——

Senator ROCKEFELLER. All others.

Secretary SAMUELS. All others. And I would mention, under our proposal, we have, on the prospective tax, a $5 million exemption so that the prospective tax does not cover a company that writes less than $5 million in premiums.

And I would also note that fire insurance on farm or owner-occupied housing units is excluded from the tax base. So I think that these small companies have only $1-5 million of premiums, and also a tax base that may not apply to policies that they write.

Senator ROCKEFELLER. All right. Thank you.

The CHAIRMAN. Thank you, Senator Rockefeller.

Your morning is about to conclude, Secretary Samuels.

Senator Daschle?

Senator DASCHLE. Thank you, Mr. Chairman.

Secretary Samuels, you anticipate that the EIRF would be extended for 10 years, requiring, as I understand it, $810 million per year, for a total of $8.1 billion over the 10-year period of time. I am interested in how you arrived at the estimate of the need, as well as the estimate of the potential, for the revenue raised. Could you clarify how you arrived at those numbers?

Secretary SAMUELS. Secretary Munnell was involved in the projections.

Senator DASCHLE. All right.

Secretary MUNNELL. Let me speak more to the expenditure side. Basically, the estimate is that there is roughly $1[illegible]on of liability out there, roughly $30 million per site tim[illegible]ential list of 3,000 sites. But this bill will reduce that lia[illegible]ity [illegible]y about 25 percent. This $8.1 billion in the first 10 years i[illegible] to pay off only 40 percent of the liability, not 100 percent. So w[illegible] are talking about paying off 40 percent of the $20 billion of liability. It is going to take some time for these projects to come on-stream.

The payments come as people actually make expenditures to clean up the sites, so we had to have a start-up for these settlements and a start-up for the clean-ups, and then some estimate for paying off past liabilities. And our sense is that, for the first 10 years, the $810 million a year should be adequate to cover the claims within that period of time.

Senator DASCHLE. That assumes 40 percent of the liability.

Secretary MUNNELL. Right.

Senator DASCHLE. But does it assume a stagnant liability? That is, that the liability that you have just described will not increase over that 10-year period?

Secretary MUNNELL. Basically, we expect all the claims to come in early in the process, so all the claims for sites that have——

Senator DASCHLE. Is that not counter intuitive? How would——

Secretary MUNNELL. The claims will come in fast. There will be a lot of paperwork processing as the policyholders demonstrate that they have some insurance and that there is an estimate of the costs that are going to be involved in cleaning up the sites.

The actual payments will take place as people make expenditures to actually do the clean-up, and that takes, unfortunately, a long period of time, so the pay-out will be slow over that period of time.

No one is arguing that this $8.1 billion is going to be adequate for cleaning up all the sites that will eventually come on the list. My sense of that is that is eventually going to cost roughly $70 billion after this bill is passed.

If the EIRF continues to pay 40 percent of that, we are talking about an eventual payment of under $30 billion over time. Without

the rest of the bill, it would cost much more. But, in the first 10 years, my sense is that the $8.1 billion should cover the costs.

Senator DASCHLE. What do you anticipate, out of a dollar spent, will be the amount attributed to legal costs and the amount actually attributed to clean-up in this estimate?

Secretary MUNNELL. Currently, 25 percent of all expenditures go for legal costs. We hope to cut that——

Senator DASCHLE. Twenty-five percent?

Dr. MUNNELL. Twenty-five percent. The number——

Senator DASCHLE. I thought it was much greater than that.

Secretary MUNNELL. The number Mr. Samuels was mentioning is of all insurance expenditures, how much goes for clean-up and how much goes for litigation. In that, his number is correct, that 88 cents on the dollar goes for litigation, 12 cents for clean-up.

But this is really a private sector project, and if you take all the private sector costs together, and you add all the litigation costs and transaction costs by the insurers, the polluting parties, and EPA, you find that 25 cents on the dollar goes to litigation and transaction costs. And we hope to eliminate almost all the litigation associated with the insurance PRP litigation, and to have a substantial reduction in the PRP litigation. So I do not see any reason why that 25 percent should not be reduced to 10. I would like to see it reduced to zero, but I am sure that some will remain.

Senator DASCHLE. Thank you.

The CHAIRMAN. You hate lawyers?

Secretary MUNNELL. I am married to one.

Senator BAUCUS. That is no answer. [Laughter.]

The CHAIRMAN. I think we had better get off this subject fast.

Thank you very much, Madam Secretary. Thank you, Mr. Secretary. You have been very informative and very forthcoming.

We are now going to hear from our panels, pro and con. Mr. Jonathan Lash, who is President of the World Resources Institute, on behalf of the Advocates for Prompt Reform of Superfund; and then Mr. W. Lawrence Wallace, Sr. will speak on behalf of the Alliance for Superfund Action Partnership. Gentlemen, we welcome you. If you have anybody you would like to bring to the table with you, they will be welcome also.

I would like to ask the committee room to come to order. I think we are getting there. I see we are going to have visuals. Good. Very well.

Good morning to you both, gentlemen. Mr. Lash, you are listed first, so would you proceed? I would appreciate if you would put your statement in the record as if read and you proceed as you wish.

STATEMENT OF JONATHAN LASH, PRESIDENT, WORLD RESOURCES INSTITUTE, ON BEHALF OF THE ADVOCATES FOR PROMPT REFORM OF SUPERFUND, WASHINGTON, DC

Mr. LASH. Thank you very much, Mr. Chairman. I appreciate the opportunity to come and talk about S. 1834. I will address myself not to the insurance provisions which are specifically before this committee, but to the background of the bill that is before you. My message is really quite simple.

Fourteen years and $15 billion ago, I was an attorney for the Natural Resources Defense Council and an advocate of strict enforcement of Superfund and a critic of the EPA's administration of that program.

Then for 6 years I ran Vermont's environmental programs and had firsthand experience with the process of trying to get sites cleaned up, and the deep frustration of dealing with the Superfund program in that process.

Indeed, by the end of that experience I concluded that, for my State, at least, it was better if sites were not on the national priority list; we could get them cleaned up more quickly, more efficiently, and more cheaply.

The CHAIRMAN. Why was that?

Mr. LASH. Because it was such án arduous process to get decisions out of the Superfund program and because the parties who were involved were so concerned about their liability that they were simply unwilling to take voluntary action. Both of those issues are ones addressed by the bill before you.

Finally, Mr. Chairman, I had the opportunity, starting in 1992, to Chair an unusual private commission, the National Commission on Superfund, which included industry chief executives, environmental, labor, citizen, State, and municipal leaders who managed to reach a consensus on very significant reform recommendations with respect to Superfund, so I have seen it from a number of different viewpoints.

My messages this morning are very, very simple. First, that reform of Superfund this year by this Congress is urgent. Second, that because of the breadth of the support for S. 1834 and the work that has been done by the Congress in recent months, even though the hour is late, reform is possible. Third, that all of the remarkable progress in recent months has been an outcome of bipartisan leadership and cooperation and the only reform that is possible is bipartisan reform.

Let me be specific. The process that has led to this piece of legislation before you is certainly different than any in my experience of working on environmental issues for some 18 years. It began with a recognition by all of the stakeholders in the debate that the Superfund program was not working.

Now, each thought it was not working for different reasons—the clean-ups were slow, they were expensive, they were unfair, they were inconsistent, transaction costs were high, and there were perverse incentives against cooperation and settlement by responsible parties—but, nevertheless, everyone concluded it was broken. That was a good starting point.

There were many efforts by different parties to develop solutions. The Environmental Protection Agency, through its advisory committee, conducted an important set of negotiations on reform opportunities.

The Industry Coalition on Superfund went a long way to developing both a consistent set of views on reform of the bill, and the insurance settlements that are before you this morning.

The National Federation of independent businesses negotiated with three leading environmental groups—the Sierra Club, the Environmental Defense Fund, and the Natural Resources Defense

Council—to work out a set of provisions to help small and very small parties deal with Superfund liability, a big and very contentious issue.

The National Commission on Superfund's most important contribution was to demonstrate that understanding, agreement and continuing cooperation among traditional adversaries was, in fact, possible.

And, while the bill before you is certainly not based exclusively on the recommendations of the National Commission, the agreement and understanding among the Commission parties has lasted and has provided some of the impetus for other parties to conclude that a much larger coalition could be built, and that is what you see before you. It is really quite an astonishing tale.

I cannot imagine anyone 2 years ago would have predicted that in a hearing before the Senate Finance Committee you would have before you a bill that was supported by the Sierra Club, Chemical Manufacturers Association, National Federation of Independent Businesses, the Natural Resources Defense Council, the Big Three automakers, the Conference of Mayors—the list is three pages long, I will not go through all of it—and that you would have a bill that was so bipartisan.

In the House, Mr. Dingell, Mr. Swift, Mr. Mineta, Mr. Applegate, worked together with Congressmen Moorhead, Oxley, Schuster, and Boehlert to produce a bill that emerged from the Energy and Commerce Committee unanimously, and by voice vote from two other committees.

In the Senate, Chairman Baucus worked closely with Senators Chafee, Durenberger, and Warner to develop a very strong consensus bill that enjoys extremely broad support.

It is late, but passage of legislation is urgent. Passage of legislation is urgent because so many parties recognize that reform is inevitable——

The CHAIRMAN. Go ahead.

Mr. LASH [continuing]. Because clean-ups will grind to a halt if the bill is not reauthorized. Parties will stop whatever cooperation is under way, waiting for new direction. The businesses who are supporters of this bill say that they will be stymied in their efforts to resolve their liabilities and, instead, face continuing litigation and maintenance cost at sites. Communities whose hopes have been raised that greater participation and quicker clean-ups can begin in the coming year will be frustrated anew.

Because so many people have concluded that this bill will make clean-ups better, faster, and cheaper, the support is broad, and, for that reason, early passage is important.

I would like to focus on just three of the areas in which the bill makes substantive changes, and only very briefly, to illustrate why——

The CHAIRMAN. Mr. Lash, take your time. You have waited patiently and we are interested to hear you, as we will be interested in hearing Mr. Lawrence.

Mr. LASH. A wonderful invitation to a lawyer who has been working on these issues for so long.

Mr. Chairman, the first issue I want to talk about is one on which you have focused considerable attention in the last 5 years.

I think you were one of the first to begin to publicly express the concern that, for all of the utility and effectiveness of our environmental laws, we often seem to focus, not on the most important problems, but simply the most visible problems, and that we have to find some system to assure that we directed our resources to the most important threats.

The CHAIRMAN. The ranking.

Mr. LASH. And you have, for two Congresses in a row, submitted legislation to try to institute some kind of ranking process.

At least for Superfund, this bill begins to move in the direction of assuring that decisions are made to make the greatest investment directed at the greatest threat, and it does that by changing the remedy selection process.

It establishes the goal of clean-up very clearly and then gives much greater flexibility at the site to make decisions to direct clean-up at the real sources of risk and hot spots, and to take a series of site-specific factors into account in making those remedy selection decisions: the availability of effective technology, the cost of that technology, the future uses of the land, and particular physical conditions that make a solution that might have worked in Site A inappropriate in Site B.

It departs from the cookie-cutter and places far greater weight on the experience and knowledge of the people at the site. I think that single change would make passage of this legislation worthwhile because it will move the process far along the road to rationality.

That process of taking real-world factors into consideration is possible politically because of another change the bill makes, which is to assure that the communities the citizens who are most affected by the sites, have an effective avenue of participation in the decision process.

That is, the communities and citizens around sites are willing to accept greater flexibility if they are assured that they will get more information and opportunities to comment on the outcomes of the management decisions.

The existing program has frustrated both communities and responsible parties alike because they feel they have no way to influence the outcome of the management decisions. They simply must take what the agency gives them at the end of the process.

S. 1834 would assure citizens early opportunities to participate, would give them the means to participate knowledgeably and effectively, and would assure that communities as well as the responsible parties were part of that process.

A number of the industry supporters of this bill have specifically urged me to say they believe that this approach will give them the opportunity to negotiate common sense, practical solutions at sites instead of dealing with frightened, angry people who simply trust no one because they have been excluded from the process. This is a very important step ahead in making sure that this process becomes one that benefits the people it is most supposed to benefit.

The third set of changes have to do with the liability system, and you have heard a good deal about that this morning. The liability system has worked to impose the costs of clean-up on polluters, and it has worked to create an important set of incentives for prospective behavior.

It is the Superfund liability system that has instigated a careful, detailed review of environmental performance as part of any major commercial land transaction, but it has also set up those perverse incentives that make voluntary cooperation almost impossible and make high transaction costs the order of the day.

This bill makes a very simple set of changes. It simply establishes an early allocation system that allows parties to take responsibility for their share of the liability without taking the risk that, in doing so, they will accept 100 percent of the liability at a multiparty site.

It sets up an allocation system outside the judicial system, provides certain guarantees that it will be prompt, and very heavy incentives to encourage all parties to participate, and assures that the fund will pay for those orphaned shares where the responsible party is no longer solvent.

That change will immediately, at multi-party sites, reduce the incentives for litigation and increase the incentives for rapid action, and means that we can expect responsible parties to step forward quickly to clean up and end their liabilities.

There has been some suggestion that a simpler solution to all of this—to the insurance problems, to the transaction costs, to the difficulties of the liability system—would be to simply repeal retroactive liability, and I wanted to conclude by briefly expressing my own skepticism about that solution.

It would, first of all, require a big tax increase, at least 140 percent. It would, second of all, make for an expensive public works program by eliminating the incentives on private parties to control costs because they are no longer paying the cleanup directly. Instead, it would eliminate one of the most effective means for assuring that clean-ups are efficient.

Third, litigation would continue. It would no longer be litigation over the current question of liability, but, instead, the litigation would be over the application of the exceptions and limits to retroactive liability: was this site before or after 1981; were these parties who violated the law?

Finally, of course, it would penalize those parties who have been most responsible, stepped forward and accepted their responsibility, paid hundreds of millions of dollars for clean-up, and now would be told that if they had simply resisted responsibility they would have been freed from those expenses and be allowed to depend on the public works program. I think it would lead to years of delay while we tried to implement a new system and is far inferior as a solution to the one that is before you.

Thank you very much, Mr. Chairman.

The CHAIRMAN. Thank you, Mr. Lash. I appreciate much of what you said there. I was on hand when the Superfund legislation was enacted in a post-election session in 1980, and it was in response to discoveries, if you will, at the Love Canal site in Niagara County, Niagara Falls, which has not had a happy record at the level of science. Nothing has ever been proven. It was just an unfortunate beginning. We did not know what we were dealing with, and are yet to have dealt with it.

And may I say, for those who wish to know about the organizations that support this measure, there are three pages in your testimony, and they will be in the record.

[The prepared statement of Mr. Lash appears in the appendix.]

The CHAIRMAN. Mr. Wallace, on behalf of the Alliance for a Superfund Action Partnership, and your associate, Mr. Bacha, is with you. Good morning, Mr. Bacha. Welcome.

Mr. BACHA. Good morning.

The CHAIRMAN. Mr. Wallace, would you proceed?

STATEMENT OF W. LAWRENCE WALLACE, SR., HAZEL & THOMAS, ON BEHALF OF THE ALLIANCE FOR A SUPERFUND ACTION PARTNERSHIP, FAIRFAX, VA, ACCOMPANIED BY ROBERT BACHA, DEPUTY EXECUTIVE DIRECTOR

Mr. WALLACE. Good afternoon, Mr. Chairman, and the committee. I am Larry Wallace, the Executive Director of the Alliance for a Superfund Action Partnership. I am pleased to have the opportunity to have been asked, through your staff, to provide some comment on the proposal that is before you to reauthorize the Superfund. I will testify primarily on the overall bill, the background, and the history, as my colleague, Mr. Lash did.

The CHAIRMAN. Good.

Mr. WALLACE. But will make a few comments about some of the impacts I feel will result if this legislation is enacted from the financing and tax point of view.

Like Mr. Lash, I have a long professional and personal history in environmental law practice. Twenty years ago I started practicing environmental law in representing a corporation.

I left that corporation to go on and head the State program in the State of North Carolina. After the Carter Administration came to Washington, I was asked to join the Justice Department here and was one of the litigators who filed the first complaints in the Love Canal case.

I also was present when the 1980 legislation was being finalized, and, from the Justice Department point of view and representing, primarily, EPA, provided assistance to the Senate and this Congress as it adopted the landmark legislation in 1980.

I stayed with the Justice Department doing environmental litigation through the late 1980's, and for the last 8 years I have represented communities, potentially responsible parties, and others, in the Superfund types of actions and other actions involving uncontrolled toxic waste sites.

The association, or Alliance Coalition that I represent this morning is the broadest, largest, and most diverse constituency representing fundamental reform for Superfund which opposes Senate bill 1834.

We have a diverse constituency. We represent fundamental reform. Our membership includes local governments, environmental activists, individual large businesses, business associations, civil rights interests, individual small businesses and their associations, environmental, as well as health professionals.

We start from the point of view that the real purpose behind the Superfund should be to protect public health. And, even in testimony before the House Public Works and Transportation Commit-

tee this summer, the GAO indicated that public health is not the top priority, that in many instances under the existing legislation, deep pockets and other priorities control.

Our membership is long and our roots, like those who support the legislation, came through the National Superfund Commission. I served as a staff person to one of the members of that commission and worked with the originator of the commission, Mike MacIntosh, who had his foundation to give the original half million dollars to start the National Commission on Superfund.

At the end of that process, however, it was Mr. MacIntosh, Dr. Chavis, and a few other members who dissented from the findings of the National Superfund Commission and went to work on finding alternative solutions that might do more to help the communities that they cared about so much.

The CHAIRMAN. Mr. Wallace, would you excuse me? The Secretary of State is calling and I sort of have to answer him, so Senator Baucus will take over for the moment and I will be back.

Mr. WALLACE. Just continue?

Senator BAUCUS. Sure.

Mr. WALLACE. Here, I will make a few important and brief points with the time allowed because, like Mr. Lash, I feel the situation is fairly simple. The ASAP coalition does not support S. 1834; we do support fundamental reform. The Administration bill has made some limited progress but falls far short of what is necessary to change the failed Superfund program in a way that will serve the national interests.

A new authorization is not required for another 12 months. We urge this committee to take the time to fix the program and to study these alternatives carefully. We offer an eight-point plan which can do this.

But let me discuss some of the major problems that we see with S. 1834. First of all, minority, people of color, urban, and poor communities are not adequately addressed. Second, public health does not receive the attention it deserves. Third, the bill legislates unfunded mandates which will rob the existing program of dollars which could be used for clean-up.

If I could address your attention to the chart at my left, you see six lines, four going in the up direction, two going in the down direction. What this chart represents at the baseline is the current $1.5 billion appropriation for the Superfund program.

The first bar, is the $700 million, maybe $800 million that would be involved in this committee approving the new EIRF tax. That would be new spending.

The second bar up, the $300 million, is that this proposal in S. 1834 would reserve $300 million of the current $1.5 billion to pay for orphan shares. Some of these orphan shares are, in fact, created by some of the benefits that are given to special interest groups in S. 1834.

In addition, the very creation of this new government EIRF bureaucracy would add approximately $50 million in additional government costs that are not currently incurred. Those are the three green bars, the $50 million, the last of the three.

In addition to that, as Mr. Lash described, there are a number of what I call unfunded mandates, promises that are made to com-

munities to have health centers, TAC grants, to increase the number of health assessments done by ATSDR, and to provide incentives for innovative remedies and to subsidize other activities that would be caused by the program.

We have made some estimates, and I think the other side would agree with those estimates, roughly, that these new areas, if funded, would cost about $160 million more a year. Now, what has already happened is that the Senate Appropriations Committee has already taken the $300 million away from the $1.5 billion, so this year EPA would have an appropriation of $1.5 billion to use for the program.

If this proposal is adopted, in the first instance they will immediately lose $300 million, then to do the EIRF, there is another $50 million, and to do all of the unfunded programs, most of which I think are good programs. But you should put the money there to do them, because if you do not, then that money, too, has to come from the fund.

So then that brings me to the last two bars, which take the negative direction. If you, in essence, take the $300 million that the Senate Appropriations Committee has already reserved for the orphan shares and added to the $50 million for the new costs, you get my fifth bar, which means you take the $1.5 billion and you take it down $350 million. When you add to that, the yellow bar, you get a total reduction from current spending levels in the Superfund program of $510 billion.

So, with the historical $1.5 billion that we have been spending—and, mind you, over the last 14 years, even at that level, that only allowed, according to EPA statistics, 237 sites to be cleaned up.

At the same time, only 1,000, 1,500 or so were listed on the MPL, and this is out of a universe of, approximately, what is estimated to be around 30,000 sites nationwide. Even at the old spending level, without these new reductions that S. 1834 causes, it would take another 1,400 years at that rate to deal with the problems that we see.

The other thing I want to focus on for a moment is, in terms of this particular $300 million that we will lose from the program, the cause in this legislation for that loss results from the special benefits that are derived.

For example, if you take the 10 percent municipal liability cap that is allowed, the way that cap is defined, a municipal solid waste generator, which does not only include municipalities but would include private waste haulers, could not get liability in a Superfund situation above that 10 percent.

If, under the current law, which I believe is the case, you could have situations where their liability would far exceed that 10 percent, then that additional liability could become a part of this orphan's share, which would be shifted from these municipalities or private interests over to being funded by the $300 million from the orphan's share.

I suggest that the committee carefully consider before adopting this legislation. In my own personal background, I grew up in the deep South in a minority community that had a Superfund site. We were not prepared, as a community, to fight that site and we needed the help of the government.

I hope that, given the situation that we currently have in our country, that three out of every five minority lives, works, or is otherwise adversely affected by uncontrolled toxic waste, that we, in our wisdom, will carefully study these solutions to provide a better answer than S. 1834.

I would suggest to each of the committee members that, prior to supporting this legislation, you ask your constituents outside the Beltway who live, work, or have businesses that are affected by these sites as to whether this would provide the solutions that the proponents suggest.

Finally, I would suggest that you might want to take a given Superfund site in your State or in close proximity and ask the real people affected by that site as to whether S. 1834 provides the answer.

My suggestion is that if you ask the real people and if you face the realities and not the myths, you will find that fundamental reform is required and not mere tinkering at the edges. Thank you.

Senator BAUCUS. Thank you, Mr. Wallace.

Mr. Lash, I am just curious what your reaction might be. As I understand your basic point, Mr. Wallace, the consequence of this legislation is that fewer resources are going to be available for clean-up. I think that is basically what you intend that chart to demonstrate. Mr. Lash, your response?

Mr. LASH. Well, I have not seen the figures on which this is based. I would note that there is certainly one portion of it that I disagree with, just on first glance, that he is pointing out the fund reserved for the orphan fund. As I understood that, that is part of the red area below the line, but, of course, the payment of orphan shares is part of clean-up.

My understanding, in working with the agency, is that they have concluded that the bill would provide more resources, not fewer resources, for clean-up and I certainly agree that the goal should be the direct resources to clean up, not the transaction costs.

Senator BAUCUS. Yes. That is where the question came to my mind, Mr. Wallace. Is it not true that one of the reasons why fewer dollars are going to be spent is because it is a consequence of the allocation system, and the EIRF, and the remedy selection, et cetera, that clean-up dollars will be spent a lot more efficiently than currently is the case. So even though there may be, on an absolute basis, fewer dollars total, on a comparative basis it is spent much more efficiently, that is, more toward clean-up.

Mr. WALLACE. I would respectfully disagree, Senator. I do not know whether Mr. Lash has seen the numbers, or whether you have or not. I think you could take judicial notice of the action that the Senate Appropriations Committee has already taken. They reduced the EPA appropriation by $300 million earlier this summer in response to the fact that this legislation exists and requires this $300 million.

I do understand, as Mr. Lash would indicate, that this $300 million would go toward clean-up, but the issue that I take with that $300 million going toward clean-up is that at least a part of that is money that under the current system would come from the private sector, and not the government, from PRPs who are relieved of responsibility by special provisions in this bill, like the 10 per-

cent cap I mentioned, like the exclusion for the banking industry, like the exclusion that would exist for the insurance industry, and other exclusions help create a new type of orphan's share.

We have always dealt with, in Superfund litigation, orphan shares, but what that used to mean was where you could not find or have a viable, responsible party to step up to the plate. But what we are suggesting here by this proposed legislation is to grant some special protections to people and then pay for that with these government dollars.

Senator BAUCUS. As I understand it, basically we are now discussing the merits of the bill which were all laid out and hashed out in the Environment and Public Works Committee at an earlier date, and the committee reported out the bill. We are here today basically on the tax, on the EIRF.

Mr. WALLACE. Well, when I was called and asked to come——

Senator BAUCUS. I understand.

Mr. WALLACE. We were specifically asked——

Senator BAUCUS. I understand.

Mr. WALLACE [continuing]. To come and talk about the general merits of the bill, not to deal with it in detail.

Senator BAUCUS. Correct.

Mr. WALLACE. But to give you some idea, before this committee acted on an important and significant financial matter, that it have some idea of what it was doing before it went forward.

Now, what I would have suggested is that, instead of this committee passing legislation that would allow for the $700 million EIRF, is that the increase taxes that amount, not to resolve disputes, but to allow those taxes to go directly into clean-up.

Senator BAUCUS. That is correct. So your basic proposal is to repeal retroactive liability and, in its place, establish a public works clean-up program. Is that correct?

Mr. WALLACE. That is incorrect.

Senator BAUCUS. What is your basic view then?

Mr. WALLACE. All right. First of all, what we would do in certain situations is provide a modification to the imposition of retroactive liability where you had a party that was involved in a multi-party site, where they, those private parties, agreed to manage the clean-up, they would be left out of the liability scheme as a lawsuit matter, they would have to pay into the tax.

The tax would then, as we set up trust funds now for Superfund sites, be allocated a certain dollar figure to work on that site. Work on the site would not be done through a public works program, but will be done by the private parties.

As a part of the condition of giving up their liability position they will still have to agree to come to the table and perform the work and do the site clean-up. So we were not looking at a continuation of the litigation or at a public works program, and we would not repeal retroactive liability.

In fact, our proposal would be more stringent than the S. 1834 proposal because S. 1834 allows the fair share or fair allocation of prospectively and retroactively, whereas, we would leave strict joint and several liability in place as you go forward to make sure all of the incentives were there for people to do the right thing going forward.

Senator BAUCUS. Well, I appreciate that, Mr. Wallace. You make some interesting points. As I earlier said, we have already hashed this bill out and hope to go to the floor complying with the EIRF proposals. I would just encourage you to keep working with all of us as we go to the floor to try to continue to improve upon this bill.

I see no other Senators here to ask questions, so I thank you very much for your testimony.

Mr. LASH. Thank you.

Mr. WALLACE. Thank you, Senator.

Senator BAUCUS. Thank you.

Now, turning to the next panel. The next panel consists of Mr. Richard Smith, president of Chubb Corporation, on behalf of the American Insurance Association; Michael Murphy, counsel to chairman, American International Group; Joseph Brandon, senior vice president and chief financial officer, General Reinsurance Corporation, on behalf of the Reinsurance Association of America; and Howard E. Steinberg, senior vice president, general counsel and corporate secretary, Reliance Group Holdings, Inc., on behalf of the National Association of Independent Insurers.

I think I will just go down the list here. Mr. Murphy, you are sitting over to our left here so I will just begin with you. Unless, Mr. Smith, you want to go first?

Mr. SMITH. Yes.

Senator BAUCUS. All right. Why don't you go ahead?

STATEMENT OF RICHARD D. SMITH, PRESIDENT, THE CHUBB CORPORATION, ON BEHALF OF THE AMERICAN INSURANCE ASSOCIATION, WARREN, NJ

Mr. SMITH. I am Richard D. Smith, president of the Chubb Corporation. Today I appear on behalf of the American Insurance Association. The AIA is comprised of 270 insurance companies which, together with the American International Group, CNA, and several other companies supporting Superfund reform, write approximately 50 percent of the insurance lines which serve as the funding base for the Environmental Insurance Resolution Fund.

The fund created in Title 8 of Senate bill 1834 creates a process for the resolution of disputes between potentially responsible parties under Superfund and their insurers.

The financing for the EIRF reflects an extraordinary compromise achieved through the efforts of several divergent interest groups. After a great deal of difficult negotiation, the approach now reflected in the Ways and Means Committee amendment was developed.

AIA and AIG agreed with that compromise and strongly support the funding reflected in the Ways and Means amendment. That compromise, in very general terms, called for a 70 percent retrospective, 30 percent prospective split in the first 4 years, and a 65 prospective, 35 percent retrospective split during the remaining 6 years.

Under the amendment, approximately 25 percent of the total $8.1 billion would be raised from domestic and foreign reinsurers. This result was an equitable distribution of the financing burden of EIRF.

The reinsurers, however, did not support the 25 percent assessment. Further constructive negotiation was entered into between the direct writers and the reinsurers, with the assistance of the Administration.

As a result of that negotiation, a new financing framework has been reached with the reinsurers for their share of the tax. That formula provides that the reinsurers will contribute a cap of $188 million each year under a rate to be established by the Joint Committee on Taxation; the direct writers will contribute a cap of $622 million each year. A consensus of insurers and reinsurers that write approximately 60 percent of the EIRF-taxable premiums now support this framework for financing EIRF.

The AIA urges this committee to pass the fund's financing in the form adopted by the Ways and Means Committee with the suggested changes in the reinsurers' and direct writers' contributions.

Testimony in other committees dramatically demonstrates that hazardous substance coverage disputes result in heavy transaction costs. Everyone who has commented on this issue believes this litigation is wasteful. These funds could be used far more productively to clean up contaminated sites.

As much as we support retroactive liability repeal, we just do not see elimination of that liability as politically possible. Accordingly, given the political reality, we believe that the fund is the best way to eliminate wasteful litigation in a manner that is equitable, both to the insurance industry and to the companies targeted as PRPs.

Enacting this bill without the funding mechanism approved by House Ways and Means and modified by the agreement by insurers and reinsurers would erode the entire spirit of total compromise reached after long and arduous negotiation with the support of the Administration.

This bill continues to be opposed or is sought to be modified still further by a number of those insurers which write a minority of EIRF-taxable premiums. Many of that group will benefit from the litigation relief provided by EIRF, but refuse to bear their fair share of financing the cost of that relief.

The $5 million exemption will eliminate the burden for many small insurers. Equity requires that those who exceed that exemption accept the responsibility to share the cost, as well as the benefit.

We in the insurance industry have been asked to help develop a bill and a funding mechanism that represents a consensus of insurers and reinsurers who will bear the bulk of the cost and receive the majority of the benefit. The framework we have proposed today is a fair response to that call for legislative action.

In closing, I urge the committee to adopt the financing arrangement which now represents that broad consensus of the industry that we have achieved through good faith negotiation over the last year.

Now, if I may, Senator, that completes my statement. I have a couple of comments, if they are of interest to you now, concerning questions that were raised earlier.

The CHAIRMAN. Please. Please do.

Mr. SMITH. First, I would say on the issue of Superfund insurance policies, no one believed—none of the companies that I had

any acquaintance with in my experience in the industry—that they were writing Superfund insurance in 1970 and earlier, and in 1970-1985.

It was the concept of retroactive liability that was introduced into the law in 1980 that caused the PRP community to become retroactively liable for activities that formerly appeared to be legal and correct that created the basis for the litigation. Those companies naturally reviewed their insurance policies, then began litigation against those insurers to try to recover the costs imposed on them by the original Superfund law of 1980.

The litigation that we are talking about today is litigation over coverage, so it does not involve jury verdicts, it involves judicial interpretation of what coverage is meant to be, or is thought to be, or presumed to be by various judges around the country who have an opportunity to pass on it by reason of the litigation before them.

So that when you come to the 20/40/60 that you were troubled with earlier in the day, that 20/40/60 is not a result of jury verdicts, but it is a result of judicial interpretation of coverage, so that if you take a particular State, such as New York, the PRPs, negotiating with the insurers, decided that New York was a State where most of the decisions were more favorable to the insurance industry and its position on coverage.

A state such as New Jersey which had a 60 percent allocation was based on the fact that most of the decisions coming out of the State of New Jersey were favorable to the PRP community in their litigation over coverage.

So the fairness of the 20/40/60 was after extended debate between those two parties who were the principal litigants in all of that litigation on coverage as to what constitutes a fair and just evaluation of where a State's decisional law came down.

The CHAIRMAN. That is very clarifying.

Mr. SMITH. I thought I might offer you that. Thank you.

The CHAIRMAN. Thank you, sir.

Just one question, out of curiosity. Is Chubb a British firm, originally?

Mr. SMITH. No. There is a Chubb Lock Company.

The CHAIRMAN. Yes.

Mr. SMITH. And we have benefited by the fact that they exist with a lot of free advertising.

The CHAIRMAN. I see.

Mr. SMITH. However, The Chubb Corporation is an American company and is incorporated in the United States, as all of its subsidiaries are.

The CHAIRMAN. So you are not an alien.

Mr. SMITH. We are not an alien. We are not even a foreigner. [Laughter.]

The CHAIRMAN. Thank you, sir.

[The prepared statement of Mr. Smith appears in the appendix.]

Now, Mr. Michael Murphy, who is counsel to chairman of the American International Group, which is, of course, a New York organization. Mr. Murphy, welcome.

STATEMENT OF MICHAEL MURPHY, COUNSEL TO CHAIRMAN, AMERICAN INTERNATIONAL GROUP, INC.

Mr. MURPHY. Good afternoon, Mr. Chairman. It is my pleasure to be here today speaking in favor of the legislation before you, the Superfund bill, and specifically the Environmental Insurance Resolution Fund.

Mr. Chairman, the package before you being presented to you represents a delicate compromise between the parties, which have spent countless hours in tedious negotiations. Before going on, I would like to thank the Administration for its leadership in bringing together those interests in the compromise. A special thanks to Les Samuels.

The CHAIRMAN. Obviously, he has worked fabulously.

Mr. MURPHY. And Peter Yu, at the White House. Without their guidance, persistence, and patience, the package before you would never have appeared and would not have been possible.

As I stated, Mr. Chairman, the proposal before you is a compromise, one with which no one affected is totally satisfied. My company, AIG, originally opposed the Administration proposal for creating funding of the EIRF because it failed to relieve joint and several liability retroactively for Superfund fights, just as Mr. Smith has mentioned, and the provision did not contain a much broader-based tax along the lines of what ASAP is presenting.

We recognize that the legislation process is really the art of the possible, however, even the earlier tax proposal of 1973 was 70 retrospective and 30 percent prospective, which was originally sent up to you in the earlier part of the year.

Even though that fell short of what our wishes were, we have negotiated in good faith and today endorsed the compromise which has been discussed in so much detail by Mr. Samuels and Mr. Smith, and it is much less favorable than the original 70/30 Administration proposal to us.

In my view, Mr. Chairman, the EIRF package being presented for your consideration is an insurance liability resolution trust fund. For those who would suggest to the committee that it is being asked to raise taxes, even though this is a tax committee, I would suggest that nowhere else in the Tax Code does revenue collection from a party result in that same party or the similar group's parties being released from liability, essentially, the legal liabilities that we have for being on these contractual insurance policies that we issued prior to 1986.

I further believe that, to the extent possible, such trust fund amounts should be collected from the interests being released from their liability, if that is at all possible, since those were the companies which collected the funds when they issued the policies and benefitted from the premiums. And that is why we have been all along a strong proponent of the retrospective portion of the assessment formula which was presented to you.

There have been several contentious and key issues that have been presented in the compromise before you. It gets difficult to follow the principles because it is, just as we said, a compromise. The parties have agreed to the proposal based on the synergy of these components remaining intact.

These provisions, just to highlight a few, are the funding for the EIRF is authorized for 10 years, with a total of $810 million to be collected each year. At the end of 10 years, no more than $8.1 billion will have been collected and the revenue measure would come before Congress again for reauthorization.

Second, the compromise package divides funding responsibility between two major categories of the insurance industry: the direct insurers and the reinsurers, or the direct insurance and reinsurance case.

The package, further, includes funding formula which assesses direct insurance company policy premiums written between 1968 and 1986, that is, the retrospective part of it, and those policies are to be written in the future, the prospective part of it.

The package provides also a funding formula within the reinsurance category that divides the funding responsibilities roughly between the domestic industry that issued reinsurance policies in the foreign segments, reflecting their respective potential liabilities that are being relieved under the trust fund settlement concept.

All separate formula categories created by the bill, as you heard from Mr. Samuels, were capped either on an annual basis or over a period of years. These formulas, again, were very hard-fought negotiations that were agreed to by all the parties that signed on to the compromise and, if changes are being made, that would result in some meaningful changes in the agreement.

The deal is that the parties that signed on, if these are meaningful changes, including the Administration itself, would withdraw their support from the segments of it. Just as we have said, it is the art of compromise and it has been a very hard-fought negotiation.

In year nine of the 10-year EIRF assessment period, the Treasury is directed to conduct a study on any of the unfunded liabilities that are remaining at the time and recommend the most appropriate form of refunding.

In its report to Congress, it is understood that the Treasury is not to draw any inference for future divisions of the assessment in any year or combination of years between the retrospective and the prospective formula that was negotiated with such difficulty in the current 10-year proposal.

In other words, the 66 percent prospective formula that we are now living with, and the 34 percent retrospective formula that will exist in year 10 cannot in any way be assumed to be the basis for the EIRF funding after year 10 because, as the Administration said, their rough estimates are that this is a 50/50 deal, so there is no inference to be drawn from what exists in year nine or year 10 that looks like it is more prospective than retrospective.

The agreement being presented to you, Mr. Chairman, is very complicated, very technical and detailed.

The CHAIRMAN. Yes. We have established that.

Mr. MURPHY. Probably because the insurance industry is such an obscure, and complicated, and technical industry to begin with.

Components of the compromise, however, are vital to the interests that are affected by the measure and are critical to continued support for the EIRF. AIG supports passage of this legislation. We

pledge to continue our cooperation and assistance to you and to the members.

The CHAIRMAN. Thank you. Thank you very much, sir.

[The prepared statement of Mr. Murphy appears in the appendix.]

Whatever else it is, we do see, as Senator Durenberger observed earlier, there was a time when we had to resolve a tax issue between the stock companies and the mutual companies, and we just gave up and said, will you resolve it? And they said, yes, we will resolve it, and they did. Things worked out pretty well, did they not?

Mr. GALE. No, it has not.

The CHAIRMAN. No, it has not worked out pretty well. [Laughter.] Well, cancel those last remarks.

Now, Mr. Joseph Brandon, who is the Senior Vice President and Chief Financial Officer of the General Reinsurance Corporation, who will speak on behalf of the Reinsurance Association of America.

Mr. Brandon, we welcome you to the Finance Committee.

STATEMENT OF JOSEPH P. BRANDON, SENIOR VICE PRESIDENT AND CHIEF FINANCIAL OFFICER, GENERAL REINSURANCE CORPORATION, ON BEHALF OF THE REINSURANCE ASSOCIATION OF AMERICA, STAMFORD, CT

Mr. BRANDON. Thank you, Mr. Chairman.

General Reinsurance Corporation is the largest domestic property/casualty reinsurer. As you noted, I am appearing today on behalf of the Reinsurance Association of America, a trade association which represents the domestic reinsurance industry.

Joining me at this hearing are 12 representatives of reinsurance companies that are headquartered in Connecticut, Kansas, New York, New Jersey, and Pennsylvania.

The CHAIRMAN. Are they here today?

Mr. BRANDON. Yes, they are.

The CHAIRMAN. Oh. Well, good afternoon. We welcome you. We wish we had seats for you, but you are very welcome to this room.

Mr. BRANDON. We appreciate the opportunity to share our concerns on the funding aspects of the Environmental Insurance Resolution Fund.

I will comment, of course, on the proposed compromise, but, first, I would like to review the domestic reinsurers' basic position on the Ways and Means proposal.

Domestic reinsurers opposed the EIRF excise taxes adopted by the Ways and Means Committee because the structure, rates, and form of those taxes unfairly discriminate against reinsurers.

Our measure of fairness is simple. The EIRF should tax reinsurance premiums in the same form and at the same rates as insurance premiums.

Prior to the Ways and Means Committee mark-up, domestic reinsurers took a position of studied neutrality on the various EIRF tax proposals for three reasons. First, domestic reinsurers were treated fairly by all of those proposals. Second, reinsurers are not direct parties to the disputes between insurers and their policyholders.

Third, our customers, the direct insurers, have been bitterly divided over each of the financing proposals under consideration.

The unfair treatment of reinsurance premiums in the Ways and Means amendment was the result of a compromise reached without our participation, despite our request to be included. Since the Ways and Means Committee mark-up, we have engaged in extensive discussions with the compromise parties and the Administration, which Assistant Secretary Samuels has previously described.

Subject to one very important condition, the domestic reinsurers have agreed to support the proposed revisions to the EIRF taxes which Mr. Samuels described. That condition, which is an essential element of the proposed compromise, is an effective retrospective tax rate on reinsurance premiums which is substantially the same as the effective retrospective tax rate on insurance premiums.

The CHAIRMAN. All right. Now, are you indicating that that is part of the present proposal?

Mr. BRANDON. Yes.

The CHAIRMAN. Yes.

Mr. BRANDON. If the rate established in the legislation meets this basic condition, and we are hopeful that it will, then the EIRF financing provisions will more nearly approximate the equitable result which we requested in our——

The CHAIRMAN. Mr. Brandon, I just want to be clear. When you say, we are hopeful that it will, what you are saying is that the present proposed legislation stays as is.

Mr. BRANDON. Yes.

The CHAIRMAN. Yes.

Mr. BRANDON. We are hopeful that the financing provisions will more nearly approximate the equitable result which we requested in our written statement of one tax rate and one tax form for all EIRF participants, primary insurers, excess insurers, and reinsurers.

While we can, with that important condition, agree to the proposed EIRF taxes, we think it is important to briefly review with you the basis of our objections to the Ways and Means proposal. We have, of course, provided a more extensive explanation in our written testimony.

The Ways and Means EIRF excise tax proposal is unfair for three reasons. First, it is unfair to require domestic reinsurers to bear all of the risks of non-payment by foreign and insolvent reinsurers. Without the EIRF, direct insurers would bear all of the risk of non-collection from their foreign and insolvent reinsurers. The EIRF should not be used to shift that burden to domestic reinsurers.

Second, the Ways and Means amendment unfairly imposes an effective retrospective tax rate on reinsurers that is more than twice the effective tax rate on direct insurers.

There is no rational basis for taxing reinsurers at a higher rate. All the credible data, including an independent actuarial report by the leading experts on environmental losses—and we would be pleased to make this report available—demonstrate that reinsurers will not bear a disproportionately large share of Superfund losses.

Since reinsurers are not expected to pay a disproportionate share of Superfund losses, they should not pay a disproportionate share of EIRF taxes.

Third, I would like to point out that it is unfair to tax reinsurers on a completely retrospective basis while only one-third of direct insurers' taxes are retrospective. A retrospective tax liability must be booked immediately and, thus, will reduce earnings and capital.

Moreover, direct insurers can pass the costs of their prospective taxes, which are 68 percent of their total EIRF taxes, through to their policyholders, while reinsurers cannot pass on any of their EIRF taxes.

Furthermore, the 100 percent retrospective tax on reinsurers is inconsistent with the underlying premise for the retrospective EIRF taxes, to place a higher tax burden on those who generally benefit from the release of liability provide for in the act.

Only one-third of the tax on direct insurers is retrospective, which implies that reinsurers receive an EIRF benefit over three times greater than direct insurers. There is simply no credible data to support that conclusion.

Our willingness to accept the proposed compromise is not a recognition by us of such a disproportionate benefit, but, rather, is a pragmatic accommodation to the parties who negotiated the compromise before our participation in the process.

In conclusion, domestic reinsurers agree with the proposed revisions to the EIRF taxes, subject to the important condition I described previously. If those revisions are not achievable or that condition cannot be met, then we simply ask that reinsurance premiums be taxed in the same form and at the same rates as direct insurance premiums.

I would be pleased to answer any questions that you may have.

The CHAIRMAN. I do want to just be clear once again that what you are saying is you want the text that is before the committee.

Mr. BRANDON. I am sorry?

The CHAIRMAN. That you support the text as it is presented, as it has come to us from the Committee on Environment and Public Works?

Mr. BRANDON. Subject to the one condition I described, yes.

The CHAIRMAN. As proposed by the Administration is what I meant to say.

Mr. BRANDON. As proposed by the Administration, subject to the one condition that the effective retrospective tax rate on reinsurance premiums is substantially the same as the effective retrospective tax rate on insurance premiums.

The CHAIRMAN. Now, is that not the purpose of the Administration? Is that not your objective?

Mr. BRANDON. It is the intent of the proposal to accomplish that result.

The CHAIRMAN. Yes. So you want what is being proposed.

Mr. BRANDON. Yes.

The CHAIRMAN. Most people who come here do not want it at all, whatever is proposed, they are against it. Mr. Brandon, you are a refreshing exception. [Laughter.]

The CHAIRMAN. You said that you have some actuarial data that would help us.

Mr. BRANDON. I believe we do.
The CHAIRMAN. Yes. We will place that in the record.
Mr. BRANDON. All right.
The CHAIRMAN. Yes. Thank you.
[The information appears in the appendix with Mr. Brandon's prepared statement.]
The CHAIRMAN. And now, the very patient Mr. Steinberg, who I think is of a different view. Mr. Steinberg is Senior Vice President and General Counsel of the Reliance Group Holdings, and he appears on behalf of the National Association of Independent Insurers. We welcome you, sir. We will place your statement in the record as if read, and you proceed just exactly as you desire.

STATEMENT OF HOWARD E. STEINBERG, ESQ., SENIOR VICE PRESIDENT, GENERAL COUNSEL, AND CORPORATE SECRETARY, RELIANCE GROUP HOLDINGS, INC., ON BEHALF OF THE NATIONAL ASSOCIATION OF INDEPENDENT INSURERS, NEW YORK, NY

Mr. STEINBERG. Thank you, Mr. Chairman. Good afternoon. I am afraid I promise to be somewhat less refreshing than my colleague, Mr. Brandon.
The CHAIRMAN. I anticipated that. We have read your statement.
[The prepared statement of Mr. Steinberg appears in the appendix.]
Mr. STEINBERG. Sir, I am the General Counsel of Reliance Group Holdings, which is headquartered in New York City. Reliance is the parent company of Reliance Insurance Company, which is a property and casualty insurer which was founded in 1817 in the City of Brotherly Love, and, thankfully, continues to issue insurance policies today.
The CHAIRMAN. 1817?
Mr. STEINBERG. Yes, sir. We are one of the oldest P&C companies in the country. We operate today in all 50 States and the District of Columbia.
Accompanying me is Jack Ramirez, who is the Chief Operating Officer of NAII, the National Association of Independent Insurers, our Insurance Trade Association, which represents 575 member companies, on whose behalf I appear today.
The CHAIRMAN. Mr. Ramirez? There you are. We welcome you to the committee, sir.
Mr. STEINBERG. I thank you, sir, for this opportunity to express our views which, as you noted, are more fully set forth in written testimony presented to you today.
First, let me say that we support Superfund reform—there are many good parts to S. 1834—but not the EIRF. It is our position that the Administration's mechanism for financing the resolution of environmental clean-up disputes is grossly unfair and is bad tax policy. It should not be adopted as proposed. Instead, NAII urges you to adopt its proposed alternative, one that builds on and improves the structure originally proposed by the Administration.
I am also authorized to state the position of NAMIC, the National Association of Mutual Insurance Companies, which has over 1,200 member companies. NAMIC opposes the EIRF. NAMIC believes that the EIRF is severely flawed and should be deleted from

the bill. If, however, Congress feels compelled to go forward with the EIRF, NAMIC would support the alternative being offered by NAII.

It is vitally important, sir, for this committee to recognize that most of this country's 3,000 insurance companies do not have Superfund coverage claims and do not support the EIRF. Indeed, only about 30 companies have over 75 percent of the claims. These few large companies will be the beneficiaries of the EIRF.

The claims against them will be quantified at 20, 40, or 60 cents on the dollar and will be settled by the fund. These companies will save the huge costs of litigating these claims and they will see their balance sheets and competitive position in the marketplace dramatically improved at the expense of their smaller competitors.

Since these companies will receive most of the benefits of the EIRF, they should pay the bulk of the tax that funds it. The principle that insurance companies that benefit should pay was originally advocated by the Administration but was abandoned in the negotiations that led to the proposal which is now before you.

Most of the insurance entities involved in the negotiations with the Administration were those representing big insurers with big Superfund liabilities. So it is no surprise that they were able to take advantage of the rest of the insurance industry.

As a member of the Ways and Means Committee said, those who sat around the table with the White House and Treasury left with less liability than they had when they walked in the door. Simply stated, this is a thinly-disguised forced bail-out of a few big companies by the rest of the industry. This is having Ford dealers bailing out General Motors.

In its zeal to rush this legislation through, Treasury represented to Congress and the press that the proposal eventually adopted by Ways and Means was "fully supported by all those insurers who support the enactment of H.R.- 3800 and S. 1834. This is simply not true.

The vast majority of the property and casualty industry is opposed to this proposal. The parties to this so called compromise agreement represent only about 26 percent of the total P&C market. My company is an excellent example of how Draconian the Ways and Means proposal is.

During the 18 years from 1968 through 1985, the period upon which a significant portion of the tax is based, Reliance Insurance wrote very little business for which it would have Superfund exposure. Our profile customer was a main street business, a hardware store, a small department store. We expect to spend less than $3 million on Superfund litigation. Nevertheless, we estimate that the proposed premium tax could cost us as much as $135 million over the next 10 years. And I heard Treasury say here this morning that the tax needs not to be $8 billion, but the tax needs to be $40 billion.

And, if I use that $40 billion as a yardstick, this tax is going to cost our company $666 million. There are many insurance companies with no exposure at all that will be required to pay large premium taxes into the fund, companies which have their home offices and their policyholders in the States the members of this committee represent.

There is a better way, if you believe that the EIRF is worth saving and that all property and casualty insurers should participate in the funding. Using Treasury's original proposal as a starting point, eliminate the retrospective portion of the tax and substitute, instead, a prospective excise tax based precisely on the amounts paid for each insurer whose claims are being settled by the fund.

Those who are benefitting will pay in proportion to that measurable financial benefit. The other 30 percent of the settlement costs will be borne by the entire industry. I submit that this is sounder tax policy and a far more equitable result.

In conclusion, what you have before you is an unfair government-mandated financial windfall for a few large insurers with liabilities at the expense of their competition with little or no liabilities. This is bad public policy and it is bad tax policy.

Treasury's original objective should be the guiding principle in allocating the burden of this tax. We have demonstrated a fair way to do that and we urge you to adopt it. If our proposal is adopted, NAII will support S. 1834. If you feel, however, that this matter cannot be adequately addressed in the short time before adjournment, then we urge you to defer action on the EIRF until next year and let the rest of the Superfund bill go forward.

Thank you for your consideration of our views.

The CHAIRMAN. Well, thank you, Mr. Steinberg. Ambiguity is not one of your strong points. [Laughter.]

It was very carefully reasoned and very helpful.

I want to apologize to the panel that you can see the committee is not in full session. This is the eve of Yom Kippur and the Senate will go in recess at 2:00, but it has been in recess since about 11:00 o'clock this morning.

All right. We have both sides of it now and we are going to have to go in the back room on this. This is something that we are going to have to think out ourselves. I think it is the case that the last negotiations really finished up around 10:00 last night.

Ms. MCCLANAHAN. 9:00 or 10:00.

The CHAIRMAN. 9:00 or 10:00. So we have heard some aspects of this proposal for the first time today, so obviously I am not going to take a vote at this point. But we thank you very much for coming. We have learned a lot and we have had very careful, very thoughtful testimony. We appreciate it very much, indeed.

M . STEINBERG. Thank you, Mr. Chairman.

[Whereupon, at 1:07 p.m., the hearing was concluded.]

APPENDIX

ADDITIONAL MATERIAL SUBMITTED

PREPARED STATEMENT OF JOSEPH P. BRANDON

My name is Joseph P. Brandon. I am a Senior Vice President and the Chief Financial Officer of General Reinsurance Corporation, the largest U.S. property and casualty reinsurer. I am speaking today for the Reinsurance Association of America ("RAA"). The RAA is a trade association of 29 professional property and casualty reinsurers.[1] All members of the RAA are domestic reinsurers or the U.S. branches or subsidiaries of non-U.S. reinsurers. Collectively, RAA member companies account for approximately 75 percent of U.S. professional reinsurers and 40 percent of the current total U.S. reinsurance market. A number of RAA member companies are represented by their senior executives at today's hearing, including:

American Re-Insurance Co., Princeton, NJ
AXA Reinsurance Co., New York, NY
Centre Reinsurance Company of New York, New York, NY
Employers Reinsurance Corp., Overland Park, KS
General Reinsurance Corp., Stamford, CT
Munich American Reinsurance Co., New York, NY
National Reinsurance Corp., Stamford, CT
North American Reinsurance Corp., New York, NY
PMA Reinsurance Corp., Philadelphia, PA
Prudential Reinsurance Co., Newark, NJ
Reinsurance Corporation of N.Y., New York, NY
Signet Star Reinsurance Corp., Florham Park, NJ

We appreciate the opportunity to share our concerns about the Environmental Insurance Resolution Fund ("EIRF") excise taxes (Title IX of S. 1834). Our concerns are straightforward. An unfair process has resulted in an inequitable tax on reinsurers. Accordingly, we cannot support the EIRF tax in its current form.

The RAA has a simple request. We do not ask for special treatment, or to be exempted from EIRF taxation. We ask only that reinsurers be treated fairly. Specifically, we are asking that reinsurance premiums be taxed in the same form and at the same rates as primary and excess insurance premiums.

Professional reinsurers are simply specialized insurance companies. Primary and excess insurers purchase reinsurance to (a) protect themselves against large losses or unusual risks, (b) achieve greater diversity within their insurance risk portfolio, and (c) properly balance the relationships between their insurance risks and capital. In a reinsurance transaction, reinsurers assist primary and excess insurers by assuming a portion of their risk in exchange for a portion of their premiums. Reinsurers' clients are primary and excess insurance companies, not insurance policyholders. Reinsurers' relationship with our primary and excess insurer clients has often been analogized to that of private bankers.

As the Congress considered various Superfund tax proposals during the past two years, reinsurers have maintained a position of studied neutrality for three basic commercial reasons: first, each of the prior EIRF proposals treated reinsurers fairly, second, reinsurers are not direct parties to the policies in dispute between primary and excess insurers and their policyholder customers, and third, our customers—the primary and excess insurers—have been bitterly divided over each proposal. Testimony at the House Ways and Means Committee hearing on July 25, 1994 demonstrated the substantial differences within the primary and excess insurance in-

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[1] A list of RAA members is shown on Attachment A.

dustry over the EIRF in general and the various tax proposals for funding the EIRF. At the hearing:[2]

- The American Insurance Association ("AIA") advocated a 100% prospective tax on insurance premiums.
- The American Insurance Group ("AIG") and the National Association of
- Mutual Insurance Companies ("NAMIC") advocated a 100% retrospective tax.
- A coalition of six primary and excess insurers lead by The Chubb Corporation supported the 70% retrospective, 30% prospective tax developed by the Administration.
- The National Association of Independent Insurers ("NAII") advocated certain changes, applicable only to property and casualty insurers and reinsurers, to the Superfund corporate environmental taxes.

Domestic reinsurers could—and still can—accept any of these tax proposals because none of them unfairly discriminates against reinsurers. To the extent that these proposals applied to reinsurers, they each taxed reinsurers at the same rate and on the same form as primary and excess insurers. Thus, the RAA did not testify before the Ways and Means Committee.

In mid-August, closed-door negotiations resulted in a primary and excess insurer "compromise" that unfairly discriminated against reinsurers. The domestic reinsurers, through RAA, asked the Administration to be included in the meetings which led to the "compromise." Unfortunately for all concerned, that request was rejected.

When those closed-door meetings started, the Administration proposal was a tax that treated insurers and reinsurers the same—one tax rate, one tax base. After those meetings, the Administration proposal based on the primary and excess insurer "compromise" singled out reinsurers for an unfair, new, and separate 100% retrospective tax at an effective rate that is over 225% higher than the effective retrospective tax rate imposed on primary and excess insurers.

The EIRF tax on reinsurance premiums is unfair to domestic reinsurers because:

- It requires domestic reinsurers to bear all of the risk of nonpayment of the tax, for whatever reason, by their foreign and insolvent reinsurer competitors even though the primary and excess insurers placed most of the business with these foreign and insolvent competitors.
- It imposes a significantly higher retrospective tax rate on reinsurers (an effective rate of .83%) than on primary and excess insurers (an effective rate of .366%).[3]

It imposes a separate and different form of tax on reinsurers (100% retrospective) than on primary and excess insurers (68% prospective, 32% retrospective).

Requiring Domestic Reinsurers to Bear All of the Risk of Nonpayment by Foreign and Insolvent Reinsurers is Unfair

The structure of the EIRF tax on reinsurance premiums will effectively result in domestic reinsurers subsidizing any shortfall in collections from foreign and insolvent reinsurers. Collections of EIRF assessments from foreign reinsurers may not be consistent with their market share because of the effects of tax treaties and trade agreements, market withdrawals, insolvencies, and corporate reorganizations. Primary and excess insurers—not domestic reinsurers—placed the bulk of the reinsurance ceded to those foreign and insolvent reinsurers. In the absence of the EIRF, primary and excess insurers would properly bear all of the risk of non-collection from their foreign and insolvent reinsurers. The EIRF should not be used to shift. that burden to domestic reinsurers.

Requiring domestic reinsurers to bear all of the risk of nonpayment of reinsurer EIRF taxes by foreign or insolvent reinsurers is unfair. It is unfair because it requires domestic reinsurers to bear the burden twice—first when the primary or excess insurers placed the business with our foreign or now insolvent competitors, and again by being forced to pay an increased assessment because those foreign or insolvent competitors can not or will not pay the EIRF tax. That risk of nonpayment should be borne by all EIRF participants, not just reinsurers, by subjecting all EIRF participants to the same rates and same form of EIRF taxes.

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[2] Please see the complete written statements of the witnesses at the Ways and Means Committee hearing for the full details and supporting reasons for their respective positions.

[3] The retrospective tax rate on primary and excess insurers included in the Ways and Means Committee amendment to the Superfund Reform Act of 1994 is 0.22% during the first four years of the EIRF. Approximately 60.2% of the total EIRF assessments on primary and excess insurers during the first four years of the EIRF are being funded through retrospective taxes. Consequently, the 100% equivalent retrospective tax rate on primary and excess insurers is .366% (.22% divided by 60.2%).

Some have suggested that domestic reinsurers should bear the risk of nonpayment by foreign reinsurers, even though they would not do so in the absence of the EIRF, because primary and excess insurers are required to bear the risk of nonpayment by foreign insurers, a risk that they also do not bear in the absence of the EIRF. While the argument has some superficial logic, there is a substantial difference in magnitude between these two risks. During the relevant years, foreign insurers had an estimated 5% share of the primary and excess insurance market, while foreign reinsurers had about a 55% share of the reinsurance market. Obviously, the risk of non-collection from foreign reinsurers would have a significantly greater impact on domestic reinsurers than the risk of non-collection from foreign insurers would have on domestic insurers. The fairest way to address the risk of non-collection from any foreign insurer or reinsurer is to allocate the risks among all EIRF participants by subjecting them to the same rate and form of EIRF taxes.

THE REINSURER EIRF TAX UNFAIRLY IMPOSES A SIGNIFICANTLY HIGHER RETROSPECTIVE TAX RATE ON REINSURERS THAN ON PRIMARY AND EXCESS INSURERS

The effective retrospective tax rate for primary and excess insurers is 0.366%, which contrasts sharply with the effective rate of 0.83% assigned to reinsurers. There is no rational basis for assigning a substantially higher retrospective tax rate to reinsurers.

The unadjusted application of the effective 0.83% reinsurer EIRF tax rate adopted by Ways and Means would result in total collections from reinsurers of approximately $585 million—$269 million just from domestic reinsurers and the assumed reinsurance departments of domestic insurers—or more than twice the $200 million targeted revenue for the reinsurance tax. Even after adjusting for certain exclusions[4] required by the EIRF provisions, the 0.83% rate will still likely generate more than double the targeted amount. In addition, as currently drafted, tax payments are not capped once the EIRF's annual revenue targets are reached.

A SEPARATE TAX ON REINSURERS IS UNFAIR

No rational basis, supported by credible data, has been established for imposing a separate and completely retrospective tax on reinsurers. In fact, both the available credible data and the reasonable inferences which can be drawn from those data show that reinsurers should be taxed on the same basis as primary and excess insurers.

The best available and most credible data for U.S. insurers and reinsurers are compiled from annual state insurance regulatory filings ("Annual Statements") by A.M. Best Company, an independent authoritative source of insurance and reinsurance industry statistics since 1899. Those data show that for the years 1968-1985 in the lines of insurance taxed by the EIRF, the domestic reinsurers' market share of premiums was about 9%, and their market share of losses was also about 9%, of the respective premium and loss totals for all U.S. insurers and reinsurers.[5] Extending that analysis through 1993, domestic insurer and reinsurer losses continue to be proportionate to their premiums. As would be expected, that means that a dollar of domestic reinsurance premium did not draw a disproportionate share of losses. In large measure that's because of the way in which losses are paid when there are a large number of insureds and insurance policies responding to an environmental loss.[6]

Some have suggested reinsurers should be taxed on a separate and different basis because they will bear a disproportionately large share of Superfund losses. The available credible data simply do not support that assertion. While there is little data available for foreign reinsurers,[7] the December 31, 1993 annual reports to shareholders and Forms 10-K filed with the Securities and Exchange Commission by a number of primary and excess insurers (including some of those at the "compromise" negotiating table) report very low or "not significant" potential reinsurance recoveries for environmental claim liabilities. Almost all of the reports say that insurance companies face "significant uncertainties" in establishing their own environmental claim liabilities.

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[4] Exclusions include premiums related to foreign risks and certain liability coverages.

[5] See Attachment B.

[6] See Attachment C for an example of how clean-up costs are allocated among various potentially responsible parties ("PRP's") and multiple years of insurance coverage at a typical Superfund site.

[7] Foreign insurers and reinsurers are generally not required to file the same financial information with state insurance regulators required of domestic insurers and reinsurers.

Since the Ways and Means Committee adopted the amendment of the Superfund Reform Act of 1994 on August 19, 1994, the three largest domestic reinsurers, on behalf of the RAA, engaged Tillinghast, an independent actuarial consulting firm that is widely recognized as the leading expert in estimating insurance company environmental losses, to estimate the likely distribution of Superfund cleanup and litigation costs between primary and excess insurers and reinsurers. Tillinghast's estimate of likely distributions of Superfund losses indicates that reinsurers are not expected to pay a disproportionate share of these costs relative to their premiums.

A DIFFERENT FORM OF TAX ON REINSURERS IS UNFAIR

The EIRF imposes a 100% retrospective tax on reinsurers instead of assessing them on the same 68% prospective and 32% retrospective split that the "compromise" parties devised for the primary and excess insurers. That retrospective tax is unfair for three reasons.

First, the reinsurers' retrospective tax liability—which represents about 12% of domestic reinsurers' estimated capital—must be booked immediately and, thus, will reduce earnings and capital.[8] The retrospective taxes on primary and excess insurers will reduce their capital by only about 1%. Their prospective tax does not require immediate booking.

Second, primary and excess insurers can pass the costs of their prospective taxes, which represent 68% of their total EIRF assessments, through to their customers. For competitive reasons, reinsurers can not pass on their retrospective taxes to their customers.[9] There is no rational reason for unfairly discriminating against reinsurers by making them pay a 100% retrospective tax and book a 10 year liability currently, which will place reinsurers at a competitive disadvantage in both the capital and insurance markets.

Third, the retrospective tax on reinsurers violates the underlying philosophy for including such a tax in the EIRF, which is to place the retrospective tax burden on those companies that generally benefit from the release of liability provided for in the Act. The parties to the "compromise" somehow determined that primary and excess insurers would receive a benefit warranting a 32% retrospective tax, and that reinsurers would receive a benefit warranting a 100% retrospective tax. In fact, the likelihood of significant EIRF liability relief for reinsurers is small in relation to their EIRF tax burden. There is no rational basis for assigning a 100% retrospective tax to reinsurers, which implies that reinsurers will receive an EIRF benefit over three times greater than the benefit to the primary and excess insurers (100% as compared to 32%).

CONCLUSION

An unfair and rushed process excluded domestic reinsurers from participating in discussions that led to the EIRF "compromise" passed by the Ways and Means Committee.

The result of that unfair process was an unfair tax on reinsurers. It is unfair to reinsurers for three reasons:

- It requires domestic reinsurers to pay additional assessments as a result of nonpayment by their foreign and insolvent competitors.
- It imposes a significantly higher retrospective tax rate on reinsurers (an effective rate of .83%) than on primary and excess insurers (an effective rate of .366%).
- It is structured as a retrospective tax only.

There is no credible evidence that would support treating domestic reinsurers differently from domestic primary and excess insurers for EIRF tax purposes. We believe the only fair way to tax reinsurers is on the same basis—tax rate and tax form (prospective/retrospective split)—as primary and excess insurers, in proportion to their share of the total U.S. primary, excess and reinsurance market. Any shortfall in expected collections should be equitably reallocated among all EIRF taxpayers in proportion to their overall market share. If the EIRF is restructured in this manner, it will treat reinsurers equitably and will no longer unfairly discriminate against them.

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[8] The provisions of the amendment sponsored by Representative Rostenkowski were a last minute attempt to mitigate this booking problem by introducing an element of uncertainty through a reconciliation fund within the reinsurer tax. Unfortunately, subsequent investigation has determined that the accounting relief provided by that approach is minimal in comparison to the difficulty of administration.

[9] Some reinsurers with significant shares in the current reinsurance market were either not in business or wrote little business during the period covered by the EIRF.

We thank you for the opportunity to present these views.

ATTACHMENT A—REINSURANCE ASSOCIATION OF AMERICA (RAA) MEMBER COMPANY LISTING

American Re-Insurance Company, Princeton, New Jersey
AXA Reinsurance Company, New York, New York
Centre Reinsurance Company of New York, New York, New York
Chartwell General Insurance Corporation of New York, Staford, Connecticut
Christiania General Insurance Corporation of New York, Tarrytown, New York
CIGNA Reinsurance Company, Philadelphia, Pennsylvania
Constitution Reinsurance Corporation, New York, New York
Employers Reinsurance Corporation, Overland Park, Kansas
Frankona America Reinsurance Company, Kansas City, Missouri
General Reinsurance Corporation, Stamford, Connecticut
Gerling Global Reinsurance Corporation, New York, New York
Kemper Reinsurance Company, Long Grove, Illinois
The Mercantile and General Reinsurance Company of America, Morristown, New Jersey
Munich America Reinsurance Company, New York, New York
NAC Reinsurance Corporation, Greenwich, Connecticut
National Reinsurance Corporation, Stamford, Connecticut
North American Reinsurance Corporation, New York, New York
PMA Reinsurance Corporation, Philadelphia, Pennsylvania
Prudential Reinsurance Company, Newark, New Jersey
Reinsurance Corporation of New York, New York, New York
San Francisco Reinsurance Company, Novato, California
Scot Reinsurance Company, New York, New York
Signet Star Reinsurance Corporation, Florham Park, New Jersey
Slandia America Reinsurance Corporation, New York, New York
Sydney Reinsurance Corporation, New York, New York
Trenwick America Reinsurance Corporation, Stamford, Connecticut
Underwriters Reinsurance Company, Woodland Hills, California
Winterthur Reinsurance Corporation, New York, New York
Zurich Reinsurance Centre, Inc., New York, New York

ATTACHMENT B

Premium Information 1968 to 1985

QUALIFIED COMMERCIAL INSURANCE COVERAGES
RELATIVE MARKET SHARES
1968-1985 NET PREMIUMS WRITTEN

(INFLATION ADJUSTED TO 1985 DOLLARS)

Year	Domestic Primary Companies: CMP	Domestic Primary Companies: Other Liability	Domestic Primary Companies: Reinsurance	Domestic Primary Companies: Total	Domestic Reinsurers: CMP	Domestic Reinsurers: Other Liability	Domestic Reinsurers: Reinsurance	Domestic Reinsurers: Total	Total Market	Primary Companies' Market Share	Reinsurers' Market Share
1968	$2,733,770	$4,295,866	$35,697	$7,065,333	$138,553	$203,452	$55,136	$397,142	$7,462,475	94.68%	5.32%
1969	3,050,602	4,662,155	37,064	7,749,821	178,573	306,157	62,569	547,299	8,297,120	93.40%	6.60%
1970	3,467,439	5,473,691	44,279	8,985,409	193,188	409,071	74,431	676,690	9,662,099	93.00%	7.00%
1971	4,211,107	6,031,646	65,423	10,308,176	224,711	402,195	126,433	753,339	11,061,515	93.19%	6.81%
1972	5,115,639	6,265,413	85,035	11,466,087	244,497	392,642	159,319	796,458	12,262,545	93.50%	6.50%
1973	5,846,033	6,211,833	132,259	12,190,124	246,714	422,580	263,726	933,021	13,123,145	92.89%	7.11%
1974	5,950,859	6,094,953	145,987	12,191,800	277,024	422,892	287,210	987,125	13,178,925	92.51%	7.49%
1975	6,028,962	5,692,116	118,556	11,839,634	316,864	464,704	249,631	1,031,199	12,870,833	91.99%	8.01%
1976	7,246,691	7,310,853	171,984	14,729,528	403,838	704,061	360,475	1,468,374	16,197,902	90.93%	9.07%
1977	8,387,216	9,347,526	195,462	17,930,203	453,537	1,034,479	413,453	1,901,469	19,831,673	90.41%	9.59%
1978	9,243,932	9,878,487	286,664	19,409,084	363,993	802,654	707,891	1,874,539	21,283,622	91.19%	8.81%
1979	9,472,770	9,086,679	260,317	18,819,765	381,790	670,863	683,293	1,735,946	20,555,711	91.55%	8.45%
1980	8,645,350	7,802,994	220,522	16,668,866	359,603	575,626	651,419	1,586,648	18,255,514	91.31%	8.69%
1981	7,749,879	6,601,025	204,752	14,555,656	343,719	504,910	590,275	1,438,904	15,994,560	91.00%	9.00%
1982	7,484,820	5,800,434	216,724	13,501,978	351,618	524,807	632,408	1,508,833	15,010,811	89.95%	10.05%
1983	7,486,943	5,559,187	191,846	13,237,976	377,579	552,282	645,888	1,575,749	14,813,725	89.36%	10.64%
1984	8,188,774	6,199,862	227,869	14,616,506	454,527	558,014	698,142	1,710,683	16,327,189	89.52%	10.48%
1985	11,492,552	10,572,927	330,187	22,395,666	604,026	971,225	862,635	2,437,886	24,833,553	90.18%	9.82%
Total	$121,803,338	$122,887,647	$2,970,627	$247,661,612	$5,914,353	$9,922,616	$7,524,336	$23,361,305	$271,022,917	91.38%	8.62%
									Arithmetic Average	91.70%	8.30%

Source: A. M. Best's Aggregates and Averages, 1969 to 1986 editions
Inflation adjustments for years 1971 to 1984 per Treasury Department Superfund proposal.
Inflation adjustments for years 1968 to 1971 per CPI.

Loss Information
1968 to 1985

QUALIFIED COMMERCIAL INSURANCE COVERAGES
RELATIVE MARKET SHARES
1968-1985 LOSSES

(INFLATION ADJUSTED TO 1985 DOLLARS)

Year	DOMESTIC PRIMARY COMPANIES				DOMESTIC REINSURERS				Total Market	Primary Companies' Market Share	Reinsurers' Market Share
	CMP	Other Liability	Reinsurance	Total	CMP	Other Liability	Reinsurance	Total			
1968	$1,647,538	$3,046,092	$25,808	$4,719,439	$82,856	$152,685	$39,863	$275,405	$4,994,843	94.49%	5.51%
1969	1,764,698	3,353,799	26,834	5,145,330	104,107	249,694	45,300	399,101	5,544,431	92.80%	7.20%
1970	1,915,331	4,030,033	31,172	5,976,536	100,844	305,797	52,400	459,041	6,435,577	92.87%	7.13%
1971	2,191,380	4,791,251	43,440	7,026,071	110,558	329,800	83,952	524,310	7,550,381	93.06%	6.94%
1972	2,708,048	5,275,984	57,059	8,041,091	116,136	337,672	106,902	560,710	8,601,800	93.48%	6.52%
1973	3,197,660	5,341,320	92,052	8,631,032	115,216	395,113	183,555	693,884	9,324,916	92.56%	7.44%
1974	3,980,370	5,845,402	112,117	9,937,890	167,598	417,394	220,577	805,569	10,743,459	92.50%	7.50%
1975	3,898,328	4,862,022	91,882	8,852,232	179,978	492,122	193,464	865,564	9,717,796	91.09%	8.91%
1976	4,388,571	5,792,434	125,377	10,306,382	218,476	611,124	262,786	1,092,386	11,398,768	90.42%	9.58%
1977	4,518,380	6,952,762	148,746	11,619,888	232,212	906,203	314,638	1,453,053	13,072,941	88.89%	11.11%
1978	4,694,781	6,917,633	229,998	11,842,413	192,552	606,806	502,603	1,301,961	13,144,374	90.09%	9.91%
1979	5,512,445	6,272,819	216,795	12,002,059	240,910	553,462	491,971	1,286,343	13,288,402	90.32%	9.68%
1980	5,334,092	6,044,461	185,725	11,564,278	246,687	428,842	477,490	1,153,019	12,717,297	90.93%	9.07%
1981	5,341,874	5,591,608	173,742	11,107,224	221,355	412,511	435,623	1,069,489	12,176,714	91.22%	8.78%
1982	5,697,188	5,638,248	190,924	11,526,360	281,295	500,142	486,322	1,267,758	12,794,118	90.09%	9.91%
1983	6,176,536	5,847,340	204,150	12,228,027	311,125	594,808	541,254	1,447,187	13,675,214	89.42%	10.58%
1984	7,771,147	7,371,636	277,772	15,420,555	473,617	787,917	744,219	2,005,753	17,426,307	88.49%	11.51%
1985	10,124,938	12,750,950	317,310	23,193,198	498,321	1,274,247	784,136	2,556,704	25,749,902	90.07%	9.93%
Total	$80,863,305	$105,725,793	$2,550,905	$189,140,002	$3,893,844	$9,356,339	$5,967,055	$19,217,237	$208,357,239	90.78%	9.22%
									Arithmetic Average	91.27%	8.73%

Source: A. M. Best's Aggregates and Averages, 1969 to 1986 editions
Inflation adjustments for years 1971 to 1984 per Treasury Department Superfund proposal.
Inflation adjustments for years 1968 to 1971 per CPI.

Premium Information
1968 to 1993

QUALIFIED COMMERCIAL INSURANCE COVERAGES
RELATIVE MARKET SHARES
1968-1993 NET PREMIUMS EARNED

(AS ORIGINALLY REPORTED)

	DOMESTIC PRIMARY COMPANIES				DOMESTIC REINSURERS						
	CMP	Other Liability	Reinsurance	Total	CMP	Other Liability	Reinsurance	Total	Total Market	Primary Companies' Market Share	Reinsurers' Market Share
1968	$795,668	$1,348,550	$11,599	$2,155,817	$44,024	$57,905	$17,916	$119,845	$2,275,662	94.73%	5.27%
1969	965,675	1,534,419	12,779	2,512,873	52,786	84,833	21,573	159,192	2,672,065	94.04%	5.96%
1970	1,162,900	1,858,853	16,105	3,037,858	65,347	133,034	27,072	225,453	3,263,311	93.09%	6.91%
1971	1,412,405	2,143,831	24,595	3,580,831	77,419	152,111	47,531	277,061	3,857,892	92.82%	7.18%
1972	1,754,486	2,366,088	33,088	4,153,662	87,090	149,078	61,992	298,160	4,451,822	93.30%	6.70
1973	2,162,351	2,518,676	54,653	4,735,680	93,276	165,221	108,978	367,475	5,103,155	92.80%	7.20%
1974	2,537,509	2,696,367	66,967	5,300,843	123,608	182,740	131,748	438,096	5,738,939	92.37%	7.63%
1975	2,916,880	2,695,269	59,278	5,671,427	145,441	219,388	124,815	489,644	6,161,071	92.05%	7.95%
1976	3,592,495	3,586,881	90,997	7,270,373	194,288	331,934	190,728	716,950	7,987,323	91.02%	8.98%
1977	4,415,542	4,836,954	109,810	9,362,306	238,483	520,048	232,277	990,808	10,353,114	90.43%	9.57%
1978	5,245,982	5,717,778	169,354	11,133,114	209,930	451,014	409,821	1,070,765	12,203,879	91.23%	8.77%
1979	6,089,286	6,082,897	174,322	12,346,505	246,305	443,632	439,361	1,129,298	13,475,803	91.62%	8.38%
1980	6,461,457	6,137,936	169,554	12,768,947	266,241	441,368	487,747	1,195,356	13,964,303	91.44%	8.56%
1981	6,423,892	5,639,098	177,951	12,240,941	291,317	440,190	511,486	1,242,993	13,483,934	90.78%	9.22%
1982	6,605,796	5,242,654	199,152	12,047,602	307,202	453,725	561,566	1,322,493	13,370,095	90.11%	9.89%
1983	6,848,156	5,203,764	177,217	12,229,137	341,476	505,768	570,282	1,417,524	13,646,661	89.61%	10.39%
1984	7,463,227	5,732,631	202,132	13,397,990	412,338	518,178	645,953	1,576,469	14,974,459	89.47%	10.53%
1985	9,758,754	8,523,052	304,012	18,585,818	551,131	794,034	769,955	2,115,120	20,700,938	89.78%	10.22%
1986	13,846,980	15,154,955	484,706	29,486,641	771,501	1,431,113	1,086,625	3,289,239	32,775,880	89.96%	10.04%
1987	15,935,109	17,994,052	320,708	34,249,869	879,593	2,081,766	1,139,220	4,100,579	38,350,448	89.31%	10.69%
1988	16,751,419	18,529,527	254,815	35,535,761	704,997	1,204,829	1,317,898	3,227,724	38,763,485	91.67%	8.33%
1989	16,808,649	17,581,132	218,273	34,608,054	593,577	941,468	1,264,977	2,800,022	37,408,076	92.51%	7.49%
1990	17,048,956	17,314,516	186,303	34,549,775	576,795	906,839	1,395,678	2,879,312	37,429,087	92.31%	7.69%
1991	16,591,163	14,551,014	210,072	31,352,249	596,014	947,180	1,492,083	3,035,277	34,387,526	91.17%	8.83%
1992	16,108,679	14,080,843	266,879	30,456,401	598,210	943,027	1,505,837	3,047,074	33,503,475	90.91%	9.09%
1993	16,096,404	14,114,580	339,744	30,550,728	700,261	1,036,732	1,676,771	3,413,764	33,964,492	89.95%	10.0[illegible]
Total	$205,799,820	$203,186,317	$4,335,065	$413,321,202	$9,168,650	$15,537,153	$16,239,890	$40,945,693	$454,266,895	90.99%	9.01%
									Arithmetic Average	91.48%	8.52%

Source: A M Best's Aggregates and Averages, 1969 to 1994 editions

Loss Information
1968 to 1993

QUALIFIED COMMERCIAL INSURANCE COVERAGES
RELATIVE MARKET SHARES
1968-1993 LOSSES on EARNED PREMIUMS

(AS ORIGINALLY REPORTED)

	DOMESTIC PRIMARY COMPANIES				DOMESTIC REINSURERS						
	CMP	Other Liability	Reinsurance	Total	CMP	Other Liability	Reinsurance	Total	Total Market	Primary Companies' Market Share	Reinsurers' Market Share
1968	$479,664	$956,457	$8,386	$1,444,507	$26,326	$43,734	$12,953	$83,013	$1,527,520	94.57%	5.43%
1969	558,800	1,104,123	9,252	1,672,175	30,774	69,060	15,619	115,453	1,787,628	93.54%	6.46%
1970	642,484	1,369,134	11,338	2,022,956	34,111	99,458	19,059	152,628	2,175,584	92.98%	7.02%
1971	734,712	1,704,184	16,331	2,455,227	38,090	124,731	31,561	194,382	2,649,609	92.66%	7.3[illegible]
1972	928,137	1,993,491	22,400	2,944,028	41,368	128,207	41,968	211,543	3,155,571	93.30%	6.[illegible]
1973	1,181,472	2,168,253	38,038	3,387,763	43,560	154,482	75,849	273,891	3,661,654	92.52%	7.48%
1974	1,696,774	2,587,564	51,430	4,335,768	74,783	180,364	101,182	356,329	4,692,097	92.41%	7.59%
1975	1,886,795	2,302,295	45,941	4,235,031	82,610	232,332	96,732	411,674	4,646,705	91.14%	8.86%
1976	2,176,400	2,842,535	66,337	5,085,272	105,110	288,119	139,040	532,269	5,617,541	90.52%	9.48%
1977	2,378,799	3,535,586	83,565	5,997,950	122,103	455,562	176,763	754,428	6,752,378	88.83%	11.17%
1978	2,664,341	4,003,881	135,925	6,804,147	111,053	340,967	290,973	742,993	7,547,140	90.16%	9.84%
1979	3,543,789	4,198,546	145,209	7,887,544	155,418	365,996	307,992	829,406	8,716,950	90.49%	9.51%
1980	3,988,246	4,754,447	143,465	8,886,158	182,641	328,819	357,518	868,978	9,755,136	91.09%	8.91%
1981	4,434,821	4,781,041	150,790	9,366,652	187,608	359,635	377,477	924,720	10,291,372	91.01%	8.99%
1982	5,028,162	5,096,922	176,061	10,301,145	245,762	432,400	431,845	1,110,007	11,411,152	90.27%	9.73%
1983	5,649,469	5,472,787	188,582	11,310,838	281,376	544,710	477,898	1,303,984	12,614,822	89.66%	10.34%
1984	7,082,602	6,816,098	246,399	14,145,099	429,656	731,667	688,586	1,849,909	15,995,008	88.43%	11.57%
1985	8,597,462	10,278,801	292,155	19,168,418	454,683	1,041,773	699,889	2,196,345	21,364,763	89.72%	10.28%
1986	8,792,832	14,291,123	476,466	23,560,421	479,102	1,651,504	855,174	2,985,780	26,546,201	88.75%	11.25%
1987	9,003,337	15,546,861	382,925	24,933,123	542,709	2,212,917	915,933	3,671,559	28,604,682	87.16%	12.84%
1988	10,000,597	15,601,862	288,705	25,891,164	342,629	1,268,685	948,886	2,560,200	28,451,364	91.00%	9.00%
1989	11,665,202	14,838,475	282,882	26,786,559	366,831	735,287	1,048,666	2,150,784	28,937,343	92.57%	7.43%
1990	12,190,004	14,197,903	299,576	26,687,483	408,948	866,938	1,085,838	2,361,724	29,049,207	91.87%	8.13%
1991	12,177,914	11,116,975	283,177	23,578,066	440,454	1,027,690	1,178,745	2,646,889	26,224,955	89.91%	10.09%
1992	14,249,964	14,658,158	425,938	29,334,060	703,445	872,300	1,332,665	2,908,410	32,242,470	90.98%	9.[illegible]
1993	12,658,783	13,507,653	361,487	26,527,923	629,447	919,581	1,224,043	2,773,071	29,300,994	90.54%	9.4[illegible]
Total	$144,391,562	$179,725,155	$4,632,760	$328,749,477	$6,560,597	$15,476,918	$12,932,854	$34,970,369	$363,719,846	90.39%	9.61%
									Arithmetic Average	91.00%	9.00%

Source: A.M. Best's Aggregates and Averages, 1969 to 1994 editions

ATTACHMENT C

Environmental Liability
NPL Dump Site Remediation

Background:

- The average clean-up costs at an NPL site is approximately $30 million.
- The average site was in operation for roughly 20 years.
- The average number of responsible parties at an NPL site is estimated to be 10.

Insurance Coverage:

- Allocates the clean-up costs over all available policy years.
- Assuming each PRP bears the same share of the clean-up costs, $150,000 is allocated to each policy year [$30 million ÷ (20 years x 10 PRPs)].
- Each year for each responsible party is assumed to be a separate occurrence.

Conclusion:

- Claim payments fill the available insurance coverages horizontally, like a "bathtub".
- High layers of insurance and reinsurance coverage are not affected, unless clean-up costs are a multiple of the average size at an NPL site, or one PRP has a disproportionate share of the clean-up costs.

Coverage Layers (000's)	Years of Insurance Coverage																		
	'61	'62	'63	'64	'65	'66	'67	'68	'69	'70	'71	'72	'73	'74	'75	'76	'77	'78	'79
$50,000																			
10,000																			
5,000																			
1,000																			
500																			
250																			
150																			

NPL = National Priority List of Superfund Sites
PRP = Potentially Responsible Party

SUPERFUND

An Analysis of the Division of Potential
Liabilities Between Insurers and Reinsurers

Prepared by:

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September 13, 1994

Distribution & Use

This report was prepared for attachment to testimony by Joseph P. Brandon, on behalf of the Reinsurance Association of America, before the Senate Finance Committee on September 14, 1994.

It should be emphasized that the parameter selections and conclusions contained herein are generalized across the entire insurance industry and are not suitable for use in any other context. In particular, they should not be applied to a specific insurance or reinsurance company without analysis of that company's book of business and reinsurance or retrocessional protections over time.

Readers are cautioned that this analysis does not address and should not be applied to the estimation of insurers' and reinsurers' total potential liabilities from all waste sites. The characteristics of non-NPL sites are substantially different from those for NPL sites and the resulting allocations are likely to be different.

Reliances

In performing our analysis, we relied on the following data and information:

- Estimated industry-wide coverage and reinsurance profiles independently provided by the three reinsurers. Tillinghast reviewed these three industry-wide coverage profiles and found that they were not inconsistent with our experience.

- Work done by and for the U.S. Environmental Protection Agency (EPA) and other governmental agencies, including
  - Records of Decision (RoDs)
  - National Priorities List (NPL) Technical Data File
  - Verbal information supplied by EPA Remedial Program Managers
  - Various other public sources (such as the Office of Technology Assessment and the National Technical Information Service)

- Public information from such sources as Superfund Week

- Summaries of environmental coverage litigation cases prepared by various law firms and insurance entities

We have employed this information without independent audit or verification. However, Tillinghast did review the data and information for reasonableness and internal consistency.

Scope

Our work addresses a very specific set of costs, as follows:

- We have included only sites that have been placed on the NPL to date (approximately 1,350 sites).
- Our estimates exclude costs associated with federal sites and significant sites operated under a federal contract, such as the Fernald Feed Materials Processing Center.
- Our analysis does not address either the potential third-party non-remediation liabilities or natural resource damages arising from Superfund sites.
- Although we have included an allowance for coverage dispute costs, our analysis does not make any provision for internal overhead costs (e.g., unallocated loss adjustment expenses).

This analysis assumes that Superfund claims run to their natural termination rather than being settled as part of policy buyouts or other negotiations. It further assumes that reinsurance coverage in these years has not been commuted or exhausted by prior claims.

We have analyzed the situation as it exists prior to any pending changes to the Superfund law.

Analysis Methodology

Overview

Our conclusions are based on two computer models:

- Tillinghast's proprietary simulation model of insured waste site liabilities, which was used to develop and record a file containing multiple simulations of the remediation costs associated with individual PRPs at each site, together with their known or simulated years of involvement; and
- An allocation program that was developed by one of the three reinsurers and reviewed for reasonableness by Tillinghast. This program allocated costs to year, layer of coverage, and the corresponding reinsurance program, using estimated industry-wide coverage profiles developed independently by the three reinsurers.

We then added overall estimates of coverage dispute costs and costs for defending insureds (allocated loss adjustment expenses) on a bulk basis, using the assumptions outlined below. Finally, we adjusted the results for the effect of successful coverage defense by the insurance industry.

Simulation of Remediation Costs

Using Tillinghast's proprietary simulation model, we estimated total remediation costs at each site based on RoDs issued to date, with additional adjustments to compensate for, among other issues, perceived inadequacies of early RoDs. We then simulated the total remediation cost at a given site from a distribution ranging from 70% to 150% of the selected point estimate; this reflects EPA's own estimate of potential variability in ultimate costs. Where no public information was available, we simulated site costs from the distribution of the selected costs for the other sites.

Where an individual PRP's percentage or dollar involvement at a site is publicly known, we utilized that information. Where shares are not known, we simulated percentage shares based on the number of publicly known "big" (i.e., Fortune 1000) PRPs and "small" (i.e., non-Fortune 1000) PRPs. On average, we assigned 85% of the costs to big PRPs, 10% to small PRPs, and 5% to the orphans' share.

Limitations

The technological, judicial, and political climates involving toxic torts such as Superfund pollution liabilities are changing. As a result, historical data cannot be used for standard actuarial projections. Therefore, the conclusions of this analysis are subject to greater uncertainty than would normally be associated with a review of insured and reinsured losses. The need to estimate insurance and reinsurance profiles across the entire population of PRPs and insurers/reinsurers introduces additional uncertainty.

While we believe that the methods and assumptions we have used are reasonable at this time, it is important to understand that they are likely to change as more information becomes available.

Although our analysis makes use of conclusions drawn from our reading of summaries of relevant legal cases, our work in this regard should not be considered to provide legal advice or to anticipate how a court may rule on an individual matter.

Allocation of Simulated Costs

The allocation of costs to year, layer, and reinsurance program was examined for exposure-like triggers, separately for each of the three coverage profiles prepared independently by the three reinsurers.

The three reinsurers were asked to estimate coverage profiles for five types of insured: Fortune 1000, Main Street purchasing primary coverage from large insurers, Main Street purchasing primary coverage from small insurers, all others purchasing primary coverage from large insurers, and all others purchasing primary coverage from small insurers. However, because there were only minor differences between the profiles for large and small primary insurers, we reduced this to three groups: Fortune 1000, Main Street, and all others.

In selecting which coverage profile to use for an individual PRP/site record, the program relied on the PRP size indicator. In general, this was the big/small size used to simulate the shares; however, approximately 280 "small" PRPs with multiple Superfund site involvements were given a "medium" indicator and used coverage from the "all other" profiles.

Sensitivity Analysis

Because there is some indication that average remediation costs at Superfund sites could decrease in the future, we ran an allocation using 80% of the originally estimated losses. The results of this were almost identical to those of the full estimated costs.

Although we produced output from 200 simulation trials, we found that, when summed over all of the sites and PRPs, the allocation results were relatively stable by simulation. As a result, we used only five of the 200 simulations in our analysis.

Time constraints prevented us from doing additional sensitivity testing, for example, on the estimated coverage profiles.

Additional Costs

We currently estimate that coverage dispute costs and defense costs (i.e., defense of the insureds against the EPA and/or other insureds) will each be approximately 20% of the total remediation costs.

It should be noted that the coverage disputes commonly deal with an insured's total site population, both NPL and non-NPL. If a PRP has a significant population of non-NPL sites, an agreement to settle its NPL costs through the EIRF may be insufficient to cause it to drop its coverage suit. Although some coverage dispute costs are paid by reinsurers, the majority of these costs are paid by the direct writers; we have judgmentally selected an 80/20 split between insurers and reinsurers.

Our experience indicates that most high layer direct and reinsurance policies are written on an "expenses inside the limit" basis, while the lower layer policies are more likely to have expenses outside the limit. This would skew the payment of defense costs, with direct writers having a greater share of these costs than of remediation costs. We have judgmentally selected an 80/20 split between insurers and reinsurers.

Successful Coverage Defense

Based on past coverage decisions, we estimate that, on an overall basis, the insurance industry can successfully deny coverage on approximately 65% of the cases. We have therefore multiplied the estimated remediation costs of both insurers and reinsurers by 0.35. This assumes that reinsurers will have the same success rate as insurers in denying coverage, i.e., that they will "follow the fortunes" of their ceding companies.

Coverage dispute costs will not be reduced by successful coverage defenses. Defense costs will be reduced but not in the same proportion as remediation costs, since the duty to defend is usually found to be broader than the duty to indemnify. We have therefore applied a judgmental adjustment of 0.50 to defense costs to reflect successful coverage defenses.

We note that the estimated division between insurers and reinsurers is relatively insensitive to the coverage "win factor" selected.

REVENUE-RELATED PROVISIONS OF S. 1834 (SUPERFUND REFORM ACT OF 1994)

Scheduled for a Hearing

by the

SENATE COMMITTEE ON FINANCE

on September 14, 1994

Prepared by the Staff

of the

JOINT COMMITTEE ON TAXATION

September 13, 1994

JCX-18-94

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INTRODUCTION

This document,[1] prepared by the staff of the Joint Committee on Taxation, provides a description of the revenue provisions of S. 1834 (Title IX of the "Superfund Reform Act of 1994"), which are scheduled for a public hearing before the Senate Committee on Finance on September 14, 1994. S. 1834 contains the Administration's Superfund reauthorization proposal. The Administration also separately submitted a proposal on May 20, 1994, and modifications thereto on August 17, 1994, to provide revenues for a proposed "Environmental Insurance Resolution Fund." That proposal was subsequently ordered reported on August 19, 1994, by the House Committee on Ways and Means (with further modifications) to be incorporated into H.R. 3800 (See H. Rept. 103-582, Part 3, August 26, 1994). The Administration's Environmental Insurance Resolution Fund revenue proposal is intended to be incorporated into Title IX of S. 1834.

Part I of the document is the legislative background of S. 1834. Part II is a summary of present-law Superfund tax provisions and the Administration's proposed Superfund revenue provisions. Part III is a description of the Administration's proposed Superfund tax extensions and the Environmental Insurance Resolution Fund and accompanying revenue provisions, which are the same as the provisions reported by the House Committee on Ways and Means as an amendment to be incorporated into H.R. 3800. (Appendix A shows the excise tax rates on certain chemicals currently subject to the Superfund tax, and Appendix B lists the taxable substances currently subject to the excise tax on imported chemicals.)

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[1] This document may be cited as follows: Joint Committee on Taxation, Revenue-Related Provisions of S. 1834 (Superfund Reform Act of 1994), (JCX-18-94), September 13, 1994.

I. LEGISLATIVE BACKGROUND

S. 1834 (the "Superfund Reform Act of 1994"), the Administration's Superfund reauthorization proposal, was introduced (by request) by Senators Baucus and Lautenberg, on February 7, 1994. The bill was jointly referred to the Committee on Environment and Public Works and the Committee on Finance for matters under their respective committee jurisdiction. S. 1834, as introduced, would extend the four present-law Superfund excise taxes through December 31, 2000, and would make conforming amendments to the Superfund Trust Fund expenditure purposes to allow financing of the revised Superfund program.

S. 1834 was ordered favorably reported, with amendments, by the Senate Committee on Environment and Public Works on August 3, 1994, and the report was filed on August 19, 1994 (S. Rept. 103-349). The Committee on Environment and Public Works did not amend Title IX ("Taxes") of the bill.

On May 20, 1994, the Administration separately submitted a proposal for the imposition of two new insurance-related "fees" (drafted as excise taxes imposed and collected under the Internal Revenue Code). On August 17, 1994, the Administration submitted to the House Committee on Ways and Means a substitute proposal for funding a proposed Environmental Insurance Resolution Fund. The substitute proposal would impose two new excise taxes and a special assessment (also imposed as an excise tax under the Internal Revenue Code) on persons issuing or bearing risks under certain insurance policies. A second special assessment was substituted for a portion of the excise taxes on reinsurers by the House Committee on Ways and Means in its amendment to Title IX of H.R. 3800 as approved on August 19, 1994. (See H. Rept. 103-582, Part 3, August 26, 1994.) The Administration intends that these new excise taxes and special assessments be incorporated in Title IX of S. 1834 as the financing source for the new Environmental Insurance Resolution Fund program.

II. SUMMARY

A. Extension of Current Superfund Taxes and Trust Fund

The Internal Revenue Code imposes four different Superfund taxes. These are--

(1) An excise tax on petroleum, imposed at a rate of 9.7 cents per barrel, on domestic or imported crude oil or refined products;

(2) An excise tax on listed hazardous chemicals, imposed at a rate that varies from $0.22 to $4.87 per ton (see Appendix A);

(3) An excise tax on imported substances that use as materials in their manufacture one or more of the hazardous chemicals described in (2) above (see Appendix B); and

(4) A corporate environmental income tax equal to 0.12 percent of the amount of modified alternative minimum taxable income of a corporation that exceeds $2 million.

The revenues from these taxes are deposited in the Hazardous Substance Superfund. These taxes generally are scheduled to expire after December 31, 1995, unless (a) the unobligated Superfund balance exceeds $3.5 billion, or (b) total Superfund tax revenues exceed $11.97 billion, at specified times before that date.

The Administration has proposed extending these taxes through December 31, 2000. The Administration also has proposed modifying the purposes for which the funds in the Hazardous Substance Superfund may be spent.

B. Proposed Environmental Insurance Resolution Fund and Excise Taxes

S. 1834 would create a new Environmental Insurance Resolution Fund program to resolve disputes between potentially responsible parties (persons potentially liable for cleanup of Superfund sites) and their insurers regarding liability for cleanup of Superfund sites. Under this program, awards would be made to potentially responsible parties in an amount generally equal to a statutory percentage of eligible cleanup costs actually incurred. In exchange, claims against insurance companies would be extinguished.

The new Environmental Insurance Resolution Fund program to be created under the bill would be financed by new excise taxes and special assessments (imposed as excise taxes) on insurance

companies. The Administration proposed the taxes in a separate transmittal to the House Committee on Ways and Means on August 17, 1994. The taxes were ordered reported by the House Committee on Ways and Means (with modifications) on August 19, 1994. (See H. Rept. 103-582, Part 3, August 26, 1994.) These taxes are as follows:

Years 1-4.--A retrospective excise tax calculated by reference to insurance premiums written during the period 1968 through 1985 would raise approximately 70 percent of projected revenues, with approximately 45 percent of total revenues coming from a tax based on net direct insurance premiums written and 25 percent of such revenues coming from a tax based on net reinsurance premiums written. The remaining 30 percent of revenues would be raised by a prospective tax on premiums written for direct insurance. Tax rates would be set to raise approximately $810 million per year.

Years 5-10.--The prospective tax rate would be increased to provide approximately 65 percent of total revenues. The retrospective tax on direct insurance would be replaced by a claims-based special assessment on direct insurers designed to raise 10 percent of total revenues ($81 million per year). The retrospective tax on reinsurance would be continued at a reduced rate of 0.14 percent, and a special assessment structured identically to that imposed on direct insurers would be imposed. These two taxes would produce the remaining 25 percent of the revenues. As in the first four years, total projected revenues would be approximately $810 million per year.

The new tax provisions would be effective on January 1, 1995, and generally would expire after December 31, 2004.

C. Tax Exemption for Environmental Insurance Resolution Fund

The Administration proposal would provide an exemption from Federal income tax to the Environmental Insurance Resolution Fund under section 501(*l*) of the Code.

III. DESCRIPTION OF PROPOSED REVENUE PROVISIONS

A. Extension of Current Superfund Taxes and Trust Fund

Present Law

Four different Superfund taxes are imposed under the Internal Revenue Code. These are in general:

(1) An excise tax on petroleum, imposed at a rate of 9.7 cents per barrel, on domestic or imported crude oil or refined products;

(2) An excise tax on listed hazardous chemicals, imposed at a rate that varies from $0.22 to $4.87 per ton (see Appendix A);

(3) An excise tax on imported substances that use as materials in their manufacture or production one or more of the hazardous chemicals described in (2) above (see Appendix B); and

(4) A corporate environmental income tax equal to 0.12 percent of the amount of modified alternative minimum taxable income[2] of a corporation that exceeds $2 million.

The Treasurv Department is required to add to the list of imported taxable substances any substance if it determines that taxable chemicals constitute more than 50 percent of the weight or value of the materials used to produce such substance (determined on the basis of the predominant method of production). The Treasury may remove from the list only those substances which meet neither test.

No tax is imposed on the sale of any taxable chemical for export. In addition, if tax was paid with respect to a taxable chemical and the chemical is used as a material in the manufacture of a taxable substance which is exported, a credit or refund (without interest) is allowed to the person who paid the initial tax.

The revenues from these taxes are deposited in the Hazardous Substance Superfund (the "Superfund"). Amounts in the Superfund generally are available for expenditures incurred in connection with releases or threats of releases of hazardous substances into

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[2] Modified alternative minimum taxable income is a person's alternative minimum taxable income, but determined without regard to the alternative tax net operating loss deduction and the deduction for the corporate environmental tax (sec. 56(d)).

the environment as described in paragraphs (1), (2), (5), and (6) of section 111(a), section 111(c) (other than paragraphs (1) and (2)), and section 111(m) of the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 ("CERCLA") (as in effect on the date of the enactment of the Superfund Amendments and Reauthorization Act of 1986).

Spending from the Superfund is discretionary spending and is subject to the discretionary spending limits established in the Budget Enforcement Act of 1990.

In general, the Superfund taxes are scheduled to expire after December 31, 1995. However, the taxes would cease to be imposed earlier if either (1) (a) the unobligated balance in the Superfund exceeds $3.5 billion on December 31, 1994, and (b) the unobligated balance is estimated to exceed this amount at the end of 1995 (assuming no Superfund taxes were imposed during 1995), or (2) if the Treasury Department estimates that more than $11.97 billion of revenues from these taxes has been credited into the Superfund before January 1, 1996.[3]

Administration Proposal

Superfund taxes

In general, the Administration proposal would extend the present-law Superfund excise taxes on petroleum, chemicals, and imported substances through December 31, 2000, and the present-law corporate environmental income tax through taxable years beginning before January 1, 2001. However, these taxes would cease to be imposed earlier if the unobligated balance in the Trust Fund exceeds $3.5 billion on December 31, 1998, or December 31, 1999, and if the Treasury Department estimated that the unobligated balance would exceed this amount at the end of December 31, 1999 or December 31, 2000, respectively, if no Superfund taxes were imposed during such year. Alternatively, no further taxes would be imposed if the Treasury Department estimated that more than $22.0 billion of these taxes had been credited into the Superfund before January 1, 2001.

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[3] Cumulative Superfund tax receipts through December 31, 1993, totaled $8.939 billion.

In consultation with the Environmental Protection Agency, the Treasury Department determined that the unobligated balance in the Superfund Fund as of September 30, 1993, was $1.625 billion.

<u>Superfund spending purposes</u>

The Administration proposal would conform the Superfund expenditure purposes to the program as modified in S. 1834. Additionally, in provisions outside the jurisdiction of the Committee on Finance, the Administration proposal would amend the current "joint and several" liability standards for potentially responsible parties (persons liable for cleanup of pollution at Superfund sites). Under the Administration's proposed changes, the liability of parties agreeing to an arbitration proceeding established under S. 1834 would be limited based on their contribution to pollution of the site to be restored. Liability for pollution by parties from whom no recovery is possible (e.g., persons no longer in existence with no successor in interest), so-called "orphan shares," would be satisfied by the Superfund through a new direct spending program (see sec. 412 of S. 1834).[6]

B. Proposed Environmental Insurance Trust Fund and Excise Taxes

<u>Present Law</u>

No excise tax is imposed on domestic casualty insurance policy premiums. An excise tax is imposed on premiums for certain foreign-based casualty insurance and reinsurance. The rate of tax is four cents per dollar of premiums paid with respect to casualty insurance and one cent per dollar of premiums paid with respect to reinsurance (sec. 4371).

Revenues from the present-law excise tax on foreign insurance are deposited in the General Fund of the Treasury. There is no trust fund or other fund for Federally sponsored settlement of private environmental insurance claims.

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[6] Under the 1990 Budget Act, new direct spending is "pay as you go" spending and is separate from spending subject to the annual discretionary spending limits. New direct spending may be offset by new revenues.

The Budget Act assumes, for purposes of determining the base line of Federal receipts, that the Superfund excise taxes are permanent, notwithstanding their current 1995 scheduled expiration. Therefore, no new revenues are recorded for extension of these excise taxes. On the other hand, the corporate environmental income tax is not assumed to be permanent for purposes of determining the baseline of Federal receipts. In the Administration proposal, a portion of the revenues from extension of this tax would be used in part to offset the cost of the new orphan share direct spending program.

Administration Proposal

Overview

S. 1834, as reported by the Committee on Environment and Public Works, would establish a new Environmental Insurance Resolution Fund (the "EIRF") to resolve disputes about insurance coverage related to cleanup of superfund sites. EIRF awards generally would consist of statutorily prescribed reimbursement percentages of eligible cleanup costs incurred by potentially responsible parties. The percentages would vary from 20 percent to 60 percent, depending on the State in which the sites were located and the litigation venue for the various sites.

Potentially responsible parties electing to receive payments from the EIRF would waive all claims against insurance companies with respect to cleanup of sites for which payments from the EIRF were made. These parties would be required to submit to the EIRF all claims related to all sites (past, present, and future) with respect to which they were potentially liable for cleanup.

The EIRF would be established as a new, tax-exempt organization,[5] and its board members would be appointed by the President.

S. 1834, as reported by the Committee on Environment and Public Works, does not include funding provisions for the EIRF; the Administration, however, has proposed that the EIRF be funded with two new excise taxes and two new assessments generally imposed with respect to commercial liability insurance, as described below. The gross revenues from these excise taxes and assessments would be deposited in the Environmental Insurance Resolution Trust Fund (the "Trust Fund"), a new trust fund established for this purpose in the Trust Fund Code of the Internal Revenue Code.

Under the Administration proposal, the EIRF and the new excise taxes and assessments would terminate unless minimum participation standards were achieved. Insurers would be required to submit to the EIRF a list of all potentially responsible parties who had filed claims against the insurer as of the date of enactment within 30 days of that date. Insurers would also be required to notify all such parties of their eligibility for resolution of their claims by the EIRF.

Each eligible party so identified would have to respond in either of two ways: (1) file a declaration of intent within 90 days of the date of enactment indicating whether it intends to

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[5] See discussion of Federal tax exemption in Part III.C., below.

accept or reject a resolution offer from the EIRF,[6] or (2) file a request with the EIRF for its applicable reimbursement percentage within 60 days of enactment. In the latter case, the EIRF would be required to respond to such requests within 150 days from the date of enactment. Parties would then be required to accept or reject participation in the EIRF within 180 days of date of enactment. If more than 20 percent of all eligible potentially responsible parties reject participation in the EIRF, the EIRF and the imposition of the excise taxes would terminate. If the rejection rate is between 15 and 20 percent of all eligible potentially responsible parties, the chairperson of the EIRF, in consultation with the EIRF board, could elect to continue or to terminate the EIRF. This determination would be required to be made within 225 days from the date of enactment.

Excise taxes and assessments

The Administration has proposed to impose two new excise taxes: a retrospective tax (including an alternative foreign excise tax) and a prospective tax. In addition, the Administration has proposed two assessments (imposed as excise taxes)--one on insurers and the other on reinsurers.[7] The retrospective tax generally would be imposed on persons that wrote certain types of commercial liability insurance during the 18-year period from 1968 through 1985 and that are engaged in any trade or business (whether or not related to the current issuance of insurance) after December 31, 1994. The tax generally would be based on the aggregate net premiums written for these types of insurance during the 18-year period. The prospective tax would be imposed on direct premiums written on or after January 1, 1995, with respect to certain insurance policies in predominantly commercial lines of business.

The assessment on direct insurers generally would be imposed on any insurer if (1) a valid insurance contract (as determined by the EIRF) issued by the insurer had been submitted by an eligible person to the EIRF, and (2) the eligible person had received a resolution payment from the EIRF during the prior four year period. The assessment on reinsurers would be imposed on any person that reinsured an assessable direct policy. Each of these taxes and assessments is described in more detail below.

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[6] If an eligible person did not respond to the first notification, the EIRF would be required to provide a second notification. If such person did not respond to this second notification within 120 days of the date of enactment, the person would be deemed to have accepted participation in the EIRF.

[7] The assessment on reinsurers was added as an amendment by the House Committee on Ways and Means. This amendment was endorsed at such time by the Administration.

Retrospective tax

In general

The retrospective tax would be imposed on any "assessable person" that engages in a trade or business (whether or not related to the current issuance of insurance). The retrospective tax would be based on the net premiums written for direct insurance and reinsurance by the assessable person (or certain predecessors in interest) during the 18-year period from January 1, 1968 through December 31, 1985 (the "base period"), with respect to certain "qualified commercial policies".

In general, a qualified commercial policy would mean any insurance policy: (1) with respect to hazards, risks, losses, or liabilities within the United States[8]; and (2) the premiums for which were reported in the applicable annual statement (or would have been reported had an annual statement been filed) as relating to the commercial multiple peril, or the "other liability" lines of business.[9]

In the case of direct insurance, the retrospective tax generally would equal the amount determined by applying an "applicable funding rate" for the calendar year to the assessable person's "adjusted base-period commercial direct premiums". For reinsurance, the retrospective tax would be determined in the same manner as for direct insurance, except that the applicable funding rate would be different. Each insurer generally would be allowed an exemption amount of $50 million,[10] which would be subtracted in determining the insurer's adjusted base-period commercial premiums.

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[8] For purposes of the excise taxes and assessments under the Administration proposal, the United States generally would include Puerto Rico, and any U.S. possessions and territories. The term "United States person", however, would have the meaning in current Code section 7701. Thus, for purposes of determining whether a person was a "United States person". the term "United States" would not include Puerto Rico, and U.S. possessions and territories.

[9] A qualified commercial policy, however, does not include any policy for which premiums were required to be reported as relating to the "other liability" line of business, if the policy either (1) did not provide any commercial coverage, or (2) did not provide any comprehensive general liability coverage or any environmental liability coverage. For example, premiums related to medical malpractice coverage would be excluded.

[10] Certain related parties would be required to share one exemption amount.

For calendar years 1995 through 1998, the annual funding rate applicable to direct insurers would be 0.22 percent and the annual funding rate applicable to reinsurers would be 0.83 percent. For calendar years after 1998, the annual funding rate applicable to reinsurers would decrease to 0.14 percent and the tax applicable to direct insurers would expire.

Assessable person

An assessable person would be defined as any person that has "commercial net premiums" (as defined below), and that is either (1) a United States person,[11] or (2) any other person that (a) is engaged in a trade or business within the United States during the calendar year; (b) has taxable income effectively connected with such trade or business; and (c) is not exempt from net basis U.S. income tax under a treaty. For example, an assessable person would include a resident of a treaty country that has a permanent establishment in the United States.

Adjusted base-period commercial premiums

An assessable person's adjusted base-period commercial direct premiums would be defined as the excess of the total commercial net premiums for direct insurance written by the person (or by certain predecessors in interest) during the base period, over an allocable portion of the exemption amount.[12] Adjusted base-period commercial reinsurance premiums would be the excess of the total commercial net premiums written for reinsurance by the assessable person during the base period, over an allocable portion of the exemption amount. These determinations would be made after the commercial net premiums from each base-period year were indexed for inflation and restated in 1985 dollars.

"Commercial net premiums" would mean the aggregate of the net premiums written from any qualified commercial policy providing insurance or allocated reinsurance,[13] and 21 percent of

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[11] See footnote 8 above.

[12] For insurers with both direct insurance and reinsurance premiums during the base period, the exemption amount is allocated between direct insurance and reinsurance based upon the proportion that the inflation-adjusted commercial net premiums for each bear to the total of such premiums.

[13] Allocated reinsurance is any reinsurance for which the net premiums written were reported on the underwriting and investment exhibit of the annual statement (or would have been reported had an annual statement been filed) as relating to a specific line of business.

the net premiums written from unallocated reinsurance.[14] Net premiums written would only be subject to tax to the extent that they are attributable to the coverage of United States risks.

The determination of the net premiums written for a year generally would be based on the underwriting and investment exhibit of the annual statement filed for that year.[15] If no annual statement is filed for a given year, the premium information would be determined on a basis consistent with the annual statement requirements applicable to such year.

Alternative tax on foreign insurance

A foreign person that is not an assessable person, and that therefore would not be liable for the retrospective tax, generally would be subject to an alternative excise tax imposed on a prospective basis (herein referred to as the "alternative foreign excise tax"). The alternative foreign excise tax generally would be imposed as a withholding tax on (1) any casualty insurance policy that covers hazards, risks, losses, or liabilities wholly or partly within the United States, and (2) any reinsurance policy with respect to such an insurance policy. For this purpose, a casualty insurance policy would be any insurance policy other than any "policy of life, sickness, or accident insurance, or annuity contract" as defined in Code section 4372(e).

The alternative foreign excise tax would be equal to one-half of one percent (0.5%) of the maximum limit of liability of the foreign insurer under the policy. The term "maximum limit of liability" generally would be defined as the total amount for which the foreign insurer (or reinsurer) would be liable if each person entitled to recover from the insurer (or reinsurer) under

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[14] Unallocated reinsurance is any reinsurance other than allocated reinsurance. During the base period, insurers could report net premiums written from reinsurance on a separate line for reinsurance and were not required to allocate such premiums by lines of business on the annual statement. The Administration has stated that the 21-percent rule is intended to approximate the amount of unallocated reinsurance attributable to the commercial multiple peril and other liability lines of business.

[15] The annual statement is the financial statement filed for State regulatory purposes, on the form approved by the National Association of Insurance Commissioners. If more than one annual statement were filed in a given year, the determination would be based on the annual statement filed with any state that reports and identifies the relevant premiums most specifically by line of business.

the policy was simultaneously entitled to the maximum recovery allowed under the policy. The maximum limit of liability under a policy would not be reduced by (1) any amount for deductibles and self-insured retentions, or (2) the amount of any reinsurance.

All persons having control, receipt, custody, disposal, or payment of any premium or other amount under the policy subject to the tax would be personally liable for withholding and remitting the tax to the Treasury Department.

Foreign persons could elect to be subject to the retrospective tax in the same manner as an assessable person (see discussion above), instead of the alternative foreign excise tax. Electing parties generally would be required to enter into a closing agreement with the Treasury Department to ensure proper computation and payment of the retrospective tax and the assessments imposed on insurers and reinsurers.[16]

Prospective tax

In general, the prospective tax would be imposed on the direct premiums written after December 31, 1994, in excess of an annual exemption amount, with respect to certain commercial insurance policies that cover hazards, risks, losses, or liabilities within the United States. The tax rate would be 0.33 percent during the period January 1, 1995 through December 31, 1998, and 0.63 percent thereafter. The determination of direct premiums written for a year generally would be based on the exhibit of premiums and losses of the annual statement for that year. The exemption amount generally would be $5 million per year. However, certain related parties would be entitled to only one exemption amount, which would be allocated among them.

The lines of business identified in the 1993 form of the annual statement approved by the National Association of Insurance Commissioners ("NAIC") that would be subject to tax under the Administration proposal are: fire, allied lines, farmowners multiple peril, commercial multiple peril, ocean marine, inland marine, financial guaranty, products liability, other liability, commercial auto no-fault, other commercial auto liability, commercial auto physical damage, aircraft, fidelity,

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[16] The House Committee on Ways and Means adopted a special rule applicable to certain foreign persons that had no adjusted base-period commercial premiums. Under this rule, a foreign person generally would not be required to enter into a closing agreement (and would not be subject to the retrospective tax or the alternative foreign excise tax) if such person filed a statement certifying to the Treasury under penalties of perjury that it had no adjusted base-period commercial premiums. Adoption of this rule has been endorsed by the Administration.

surety, glass, burglary and theft, and boiler and machinery.[17] Thus, as shown on the exhibit of premiums and losses on the 1993 NAIC annual statement form, lines of business that would not be subject to the prospective tax are: multiple peril crop, homeowners multiple peril, mortgage guaranty, medical malpractice, earthquake, accident and health, workers' compensation, private passenger auto no-fault, other private passenger auto liability, private passenger auto physical damage, and credit.

Premiums written for directors and officers liability insurance, professional liability insurance, and fire insurance on residential or farm owner-occupied housing units would not be subject to the prospective tax, even though those premiums are required to be reported on the annual statement as relating to a listed line of business.

Assessments on direct insurers and reinsurers

Beginning on January 1, 1999, a portion of the EIRF's revenues would be raised by assessments imposed on direct insurers and reinsurers. The assessments would be imposed by reference to EIRF awards paid with respect to policies issued during prescribed prior periods by the insurer (or certain predecessors in interest). Each direct insurer's or reinsurer's assessment would be determined annually. These assessments would be imposed as excise taxes under the Internal Revenue Code.

Assessment on direct insurers

The assessment on direct insurers would be determined by multiplying an insurer's annually-determined "EIRF-certified percentage" by $81 million. The EIRF-certified percentage of each insurer would be determined by dividing the coverage limits on all assessable direct policies of that insurer by the aggregate coverage limits of all such policies of all direct insurers. Generally, the coverage limit of an assessable direct policy would be the aggregate limit on coverage under the policy.

An assessable direct policy would be an insurance contract (1) that has been presented to the EIRF in connection with a claim for an award, (2) that the EIRF has determined to be a valid contract, and (3) with respect to which the EIRF has made

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[17] These lines of business and those listed in the following sentence are based on the 1993 form of the annual statement as approved by the NAIC. The Treasury Department would be granted authority to designate additional lines of direct insurance business, on a prospective basis, to be subject to the tax in order to preserve the inclusion of premiums for types of insurance coverage intended to be subject to the prospective tax.

one or more resolution payments to an eligible party (e.g., a potentially responsible party) during any of the four calendar years preceding the year in which the assessment is imposed.

The EIRF would be required to identify to each insurer its assessable direct policies for each year, and to permit the insurer to identify which, if any, of those policies was reinsured. The coverage limit of any assessable direct policy would be reduced by 80 percent of the amount of any reinsurance.[18] This reduction also would be reflected in the aggregate limits on all assessable direct policies for purposes of determining the EIRF-certified percentage.

Assessment on reinsurers

The assessment on reinsurers would be determined by multiplying each reinsurer's annually-determined "EIRF-certified percentage" by $167 million. The EIRF-certified percentage for each reinsurer would be determined by dividing the coverage limits on all assessable reinsurance policies of that reinsurer by the aggregate coverage limits on all such policies of all reinsurers.

An assessable reinsurance policy would be any reinsurance policy issued by an assessable person and identified by an insurer as reinsuring an assessable direct policy. As with assessable direct policies, the EIRF would be required to identify to each reinsurer its assessable reinsurance policies for each year, and to afford the reinsurer an opportunity to contest whether the policy was reinsured and to identify which, if any, of those contracts was the subject of further reinsurance. An 80-percent deduction for reinsurance similar to that provided under the assessment on direct insurers would be provided.

Administrative matters; judicial review

The EIRF would be required to determine the EIRF-certified percentages and to report them to the Treasury Department no later than August 1 of each calendar year in which the assessments were imposed. The Treasury Department then would be required to notify insurers of the amount of their assessments, which would be payable no later than September 30 of each year.

Consistent with the provisions of Title VIII of S. 1834, the determinations made by the EIRF of EIRF-certified percentages would not be subject to judicial review. Similarly, the final

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[18] This reduction would not be allowed if the reinsurer and the reinsured were members of the same controlled or commonly managed group.

percentages would not be subject to review by the Department of the Treasury in any administrative proceeding.

Establishment of Environmental Insurance Resolution Trust Fund

The Administration proposal would establish a new Environmental Insurance Resolution Trust Fund (the "Trust Fund") in the Trust Fund Code of the Internal Revenue Code. The Trust Fund would receive deposits of the gross receipts from the new excise taxes (including the assessments), as well as any regulatory filing fees authorized under Title VIII of S. 1834 and recoveries of certain amounts by the EIRF.

Amounts in the Trust Fund would be used to fund the new direct spending authorized for the EIRF by Title VIII. The liability of the United States for all obligations under the EIRF would be limited to an amount equal to the excise taxes, assessments, and other revenues deposited in the Trust Fund. Also, the Trust Fund would be the sole source of payment for all activities of the EIRF. The Trust Fund would not be permitted to borrow from the Treasury.

Effective Dates

The retrospective tax (other than the alternative foreign excise tax) would be effective on January 1, 1995. The prospective tax would apply to policies for which direct premiums were written on or after January 1, 1995. The assessment on insurers and reinsurers would be imposed beginning in calendar years after 1998. The alternative foreign excise tax would apply to policies for which premiums were written after the close of the contingency period specified in section 816 of S. 1834 (i.e., 225 days after the date of enactment).

Notwithstanding the preceding paragraph, the imposition of all of the new excise taxes and assessments would not take effect unless the EIRF program under Title VIII of S. 1834 is in effect on August 15, 1995, and the contingency period has expired by such date. As discussed above, the EIRF program under Title VIII would terminate if certain minimum levels of participation by potentially responsible parties in the EIRF program were not achieved by the end of the contingency period.

All of the new excise taxes (other than the alternative foreign excise tax) and the assessments would terminate after December 31, 2004. The alternative foreign excise tax would terminate 10 years after the date that such tax first takes effect.

C. Tax Exemption for Environmental Insurance Resolution Fund

Present Law

Federal tax exemption for an instrumentality of the United States that is organized on or after July 18, 1984, may be provided only by an amendment to the Internal Revenue Code or by a provision enacted as part of a revenue act (sec. 501(c)(1)). Tax-exempt status has previously been granted to the following U.S. instrumentalities: (1) the Central Liquidity Facility; (2) the Resolution Trust Corporation; and (3) the Resolution Funding Corporation (sec. 501(*l*)).

Administration Proposal

The Administration proposal would provide an exemption from Federal income tax to the Environmental Insurance Resolution Fund under section 501(*l*) of the Code.

Effective Date

The proposal would be effective on January 1, 1995.

APPENDICES

Appendix A.--Present-Law Excise Tax Rates on Certain Chemicals for the Hazardous Substance Superfund

Feedstock chemical (sec. 4661)	Tax, per ton
Acetylene	$4.87
Benzene	4.87
Butane	4.87
Butylene	4.87
Butadiene	4.87
Ethylene	4.87
Methane	3.44
Naphthalene	4.87
Propylene	4.87
Toluene	4.87
Xylene	4.87
Ammonia	2.64
Antimony	4.45
Antimony trioxide	3.75
Arsenic	4.45
Arsenic trioxide	3.41
Barium sulfide	2.30
Bromine	4.45
Cadmium	4.45
Chlorine	2.70
Chromium	4.45
Chromite	1.52
Potassium dichromate	1.69
Sodium dichromate	1.87
Cobalt	4.45
Cupric sulfate	1.87
Cupric oxide	3.59
Cupruous oxide	3.97
Hydrochloric acid	0.29
Hydrogen fluoride	4.23
Lead oxide	4.14
Mercury	4.45
Nickel	4.45
Phosphorus	4.45
Stannous chloride	2.85
Stannic chloride	2.12
Zinc chloride	2.22
Zinc sulfate	1.90
Potassium hydroxide	0.22
Sodium hydroxide	0.28
Sulfuric acid	0.26
Nitric acid	0.24

Appendix B.--List of Taxable Substances Subject to the Excise Tax on Certain Imported (Chemical) Substances (Secs. 4671-4672)

Taxable substance	Taxable substance
Initial Items Listed	
Cumene	Ethylbenzene
Styrene	Methylene chloride
Ammonium nitrate	Polypropylene
Nickel oxide	Propylene glycol
Isopropyl alcohol	Formaldehyde
Ethylene glycol	Acetone
Vinyl chloride	Acrylonitrile
Polyethylene resins, total	Methanol
Polybutadiene	Propylene oxide
Styrene-butadiene, latex	Polypropylene resins
Styrene-butadiene, snpf	Ethylene oxide
Synthetic rubber, not containing fillers	Ethylene dichloride
	Cyclohexane
Urea	Isophtalic acid
Ferronickel	Maleic anhydride
Ferrochromium nov 3 pct.	Phtalic anhydride
Ferrochrome ov 3 pct. carbon	Ethyl methyl ketone
Unwrought nickel	Chloroform
Nickel waste and scrap	Carbon tetrachloride
Wrought nickel rods and wire	Chromic acid
Nickel powders	Hydrogen peroxide
Phenolic resins	Polystyrene homopolymer resins
Polyvinylchloride resins	Melamine
Polystyrene resins and copolymers	Acrylic and methacrylic acid resins
Ethyl alcohol for nonbeverage use	Vinyl resins
	Vinyl resins, NSPF

Appendix B.--List of Taxable Substances Subject to the Excise Tax on Certain Imported (Chemical) Substances (Secs. 4671-4672)--Continued

Taxable substance	Taxable substance
Additional Items Listed[1]	
1,3 butylene glycol	Methyl isobutyl ketone
1,4 butanediol	Monochlorobenzene
2-ethyl hexanol	Normal butyl acetate
2-ethythexyl acrylate	Normal propyl acetate
2,2,4-trimethyl-1,3-pentanediol diisobutyrate	Ortho-dichlorobenzene
2,2,4-trimethyl-1,3-pentanediol monoisobutyrate	Ortho-nitrochlorobenzene
Acetic acid	Para-dichlorobenzene
Acetylene black	Para-nitrochlorobenzene
Adipic acid	Para-nitrophenol
Alpha-methylstyrene	Parformaldehyde
Allyl chloride	Pentaerythritol
Aniline	Perchloroethylene
Benzaldehyde	Phenol
Benzoic acid	Poly (69/31 ethylene/ cyclohexylenedimethylene terephthalate)
Bisphenol-A	Poly (96.5/3.5 ethylene/ cyclohexylenedimethylene terephthalate)
Butanol	Poly (98.5/1.5 ethylene/ cyclohexylenedimethylene terephthalate)
Butyl acrylate	Polyalphaolefins
Decabromodiphenyl oxide	Polybutene
Dimethyl terephthalate	Polycarbonate
Diphenyl oxide	Polyethylene terephtalate pellets
Diphenylamine	Propanol
Di-n-hexyl adipate	Sodium nitriolotriacetate monohydrate
Di-2 ethyl hexyl phthalate	Tetrachlorophthalic anhydride
Epichlorohydrin	Tetrahydrofuran
Ethyl acrylate	Terephthalic acid
Ethyl chloride	Tetrabromobisphenol-A
Ethylene dibromide	Trichloroethylene
Formic acid	Trimethylolpropane
Glycerine	Vinyl acetate
Hexamethylenediamine	
Isobutyl acetate	
Isopropyl acetate	
Linear alpha olefins	
Methyl acrylate	
Methyl chloroform	

1 Items listed after enactment of the tax on imported chemical substances. The "initial" chemicals are specified in the Internal Revenue Code. The "additional" chemicals have been added to the list of taxable imported substances pursuant to the Treasury Secretary's authority.

PREPARED STATEMENT OF JONATHAN LASH

Good morning. My name is Jonathan Lash and I am President of the World Resources Institute, a policy research center that strives to provide objective information and practical proposals for policy change that will foster environmentally sound development. Thank you for allowing me the time to briefly review the history and substance of S. 1834, the Superfund Reform Act of 1994.

I have been involved in the debate over Superfund since its passage. I was an attorney for the Natural Resources Defense Council and an advocate for aggressive implementation and strict enforcement of Superfund legislation. Later, I as Vermont Commissioner of Environmental Conservation and then Secretary of Natural Resources I managed a state cleanup program and learned first hand how hard it was to deal with the Superfund program and implement practical and expeditious solutions at contaminated sites. During 1992 and 1993 I chaired the National Commission on Superfund, a group chief executives representing large and small businesses, municipalities, environmental, citizen and labor organizations.

There are three messages that I would like to leave with you today:

1. Reform of Superfund this year by this Congress is urgent.
2. Because of the very broad support for S. 1834, reform of Superfund this year by this Congress is possible.
3. The remarkable progress that Congress has made on Superfund reform in recent months has been a product of strong bi-partisan leadership, and the only reform that is feasible is bi-partisan reform.

The Superfund Reform Act of 1994 is the product of a different process than any other piece of environmental legislation that I am aware of. I hope that this process is the harbinger of a changed policy process that will shape the next generation of environmental legislation. The process began with a widespread recognition that the current program is not achieving the Nation's goal of protecting human health through efficient, effective and expeditious cleanup of Superfund sites.

Specifically, progress on cleanups has been slow and expensive. Cleanup goals and standards vary from site to site. Different communities receive different levels of protection. Transaction costs are high. The stakeholders who are most directly affected by site management decisions—local citizens, responsible parties and local government—perceive that they are excluded from the decision process. The liability system encourages litigation rather than cooperation and voluntary action.

For all of the positive results of Superfund, and there are many, the debate over reauthorization began with startlingly wide agreement, at least in what the stakeholders said in private, that significant reform was necessary.

The coalition that now supports both S. 1834 and HR 3800, the House version of the Superfund Reform Act of 1994 is the result of over two years concentrated efforts by the program's many stakeholders to develop a consensus-based series of proposals and reforms. This is not the usual, inside-the-beltway "coalition" developed overnight on a word processor in a law firm or public relations firm.

Among the settings in which the various components of the legislation were developed prior to the extensive congressional review and refinement were:

- The National Commission on Superfund. The important contribution of the Commission was to demonstrate that understanding, trust, agreement and cooperation were possible across a very broad range of Superfund stakeholders. The Commission reached agreement on recommendations for significant reform and then continued to cooperate in the legislative process, providing at least some impetus for the far larger coalition that has been built upon the efforts of many organizations.
- The EPA solicited input from the National Advisory Council for Environmental Policy and Technology (NACEPT) committee on Superfund reauthorization. This committee also included representatives from all the major stakeholder groups. These recommendations provided the foundation for the Administration's original bill introduced in February of this year.
- The Coalition on Superfund, an ad-hoc group of business and insurance companies helped forge the compromise that led to the Environmental Insurance Resolution Fund which is the principal subject of today's hearing.
- A broad coalition of city, county and state organizations worked closely with the Chemical Manufacturers Association, the environmental community and other business community representatives to fashion a compromise position for the municipalities in the liability title of the bill.
- Cleansites, a non-profit organization chaired by former EPA Administrator Reilly and involved in the cleanup of Superfund sites in more than 35 states, issued a series of recommendations that closely mirror the bill and has also endorsed the bill.

- The NFIB, Printing Industries of America and Small Business Legislative Council joined forces with the Environmental Defense Fund, The Natural Resources Defense Council and the Sierra Club to submit jointly a series of recommendations to resolve small business concerns with the Superfund program that have been incorporated in the bill.

Each of these efforts was long and sometimes contentious. Many were novel and difficult discussions among traditional adversaries. Each ultimately led various parties move away from long held positions to find solutions that met the legitimate concerns of other stakeholders. Consider the improbable alliance that has resulted from those efforts. To list just a few examples:

The Sierra Club
The Chemical Manufacturers Association
The National Federation of Independent Businesses
The Natural Resources Defense Council
The American Automobile Manufacturers Association
The U.S. Conference of Mayors
The Environmental Defense Fund
The American Bankers Association
The American Insurance Association
The National Association of Towns and Townships
The National Wildlife Federation

The list, which I have appended to my testimony, goes on for several pages. It does not include everyone. There are dissenters on the left and on the right. But it does include a very wide spectrum of the middle. Two years ago no one would have predicted that you would be marking up significant Superfund reform legislation that enjoyed support from that collection of interests.

Congress itself has spent considerable time and effort in preparing for the reauthorization of the Superfund program and has moved quickly. Through the legislative process of the past few months the initial legislation has been substantially altered and improved by both the House of Representatives and the Senate Environment and Public Works Committee. The process has been bi-partisan. In the House, Chairman Dingell, Swift, Mineta and Applegate were joined by Congressmen Moorhead, Oxley, Schuster and Boehlert from the minority side, in supporting the legislation. All three committees reported the legislation with strong bi-partisan votes with the Energy and Commerce Committee voting unanimously to pass the bill.

In the Senate Environment and Public Works Committee, Senators Chafee, Durenberger and Warner joined Chairman Baucus in shaping a bi-partisan bill. Several members of this Committee have also expressed strong support for passage of a Superfund Reform bill this year, including Senators Breaux, Danforth and Roth.

It is very late in the session for action on a bill which has not yet passed either house of Congress, but action is urgent and it is possible. The failure to reform and reauthorize Superfund this year would be expensive and chaotic. Litigation would continue, but cleanups would grind to a halt. The businesses who support S. 1834 have warned that their efforts to move forward on cleanups will be stymied while they wait for direction as their costs continue to rise.

The many, many businesses and organizations that support S. 1834 do so because they are convinced that it will make Superfund cleanups better, faster, fairer and cheaper. The breadth of the support for S. 1834 makes action this year plausible. The reasons behind that support make action this year urgent.

The reason this legislation has garnered such strong support in Congress, I believe, is the result of both the process I have briefly described above and the fact that the bill represents substantial and genuine reform of a very troubled program. While I have attached to my testimony two different summaries of the Senate legislation, one a narrative provided by the staff of the Environment and Public Works Committee and the other a Q&A developed by the coalition in support of the bill, I would like to briefly discuss three major improvements contained in the bill.

Chairman Moynihan has for years expressed the concern that the Nation's environmental laws do not necessarily focus our environmental protection efforts on the most important environmental threats. At least for Superfund S. 1834 would respond to that concern, reforming the remedy selection process to allow a response tailored to address the real sources of risk. The bill would clarify the health protection goal of cleanups, focus efforts on "hot spots," and considerably expand the flexibility of the Agency to take future land use, technological constraints, site conditions and cost into consideration.

One key reason why those changes have won the support even of local citizen groups is that they are linked to increased transparency and improved access to the process. Communities and their representatives gain the opportunity for a greater role in remedy selection through earlier and more meaningful participation in the

decision-making process. This contrasts sharply with current law whereby communities are only involved after a remedy selection has been decided by the Agency. This will provide the opportunity for intervention on the basis of data and understanding instead of fear and anger. It will allow communities and responsible parties to work together to. develop practical and common sense solutions adapted to the problems of a particular site.

Finally, the changes that S. 1834 would make in the liability system which would encourage responsible parties to accept responsibility for their share of the contamination at a multi-party site without risking the imposition of liability for the shares of other parties on them, changes the powerful incentives for litigation in the current program. That together with provisions to protect so-called "de minimis and de micromis" parties will go far to reduce unfairness in the system and encourage voluntary action.

Proposals to eliminate retroactive liability entirely continue to attract some support. The conversion of Superfund to a public works program will not fix it, they will just shift the cost to a new tax, and it would have to be a big tax. The prospect of the elimination of liability would wreck havoc on the current cleanup process, while the actual shift to a public works program would cause years of delay and increased cost.

The broad coalition that supports S. 1834 does not think that the resulting program will be perfect, only that it will work well enough so we can get on with the job at hand more quickly, more sensibly and at less cost. That would be important progress.

Thank you.

SUPERFUND REFORM:
SUMMARY OF S. 1834 - THE SUPERFUND REFORM ACT OF 1994
AS REPORTED BY
THE COMMITTEE ON ENVIRONMENT AND PUBLIC WORKS

The Superfund program is deeply troubled. Complex litigation diverts scarce resources. Cleanups are costly and slow. Community groups are frequently ignored, and poor communities are left exposed to greater hazards than affluent communities. In response, President Clinton, business leaders, community leaders, environmental leaders, and many others have urged Congress to reform Superfund.

MAJOR OBJECTIVES OF THE BILL

To bill reported by the Committee on Environment and Public Works responds to each of these major criticisms and reflects the judgment of the Committee that major improvements are needed in the Superfund program. To this end, the bill has three primary objectives: (1) to increase the involvement of States and local communities in every aspect of the Superfund cleanup process; (2) to reduce transaction costs associated with the program; and (3) to reform the remedy selection process to produce faster, better, and cheaper cleanups.

Promoting Community and State Participation

Title I of the bill increases the opportunity for communities affected by Superfund sites to have a direct and meaningful role in the cleanup process. It provides for the establishment of Community Working Groups at every Superfund site, so that the people who are the most affected by these sites will have more input into clean-up decisions. The bill establishes ombudsmen and authorizes the establishment of Citizen Information and Access Offices (CIAO) to provide needed information to communities struggling to cope with a Superfund site. In addition, the bill responds to environmental justice concerns that have been raised under the current Superfund program by requiring a study and report to Congress regarding race, ethnicity, and other socioeconomic characteristics of communities affected by Superfund sites. The bill also provides enhanced authorities to add sites in disadvantaged communities to the National Priorities List.

Title II of the bill ensures that States will also have a larger role in the Superfund program. It authorizes the delegation of CERCLA authorities to

qualified States so they can implement the cleanup of National Priority List sites under Federal law.

Slashing Litigation

One of the most controversial aspects of the Superfund program is its liability system, which is based on common law and the principle that the polluter pays. Under the strict, joint and several, retroactive liability scheme, anyone who contributed a hazardous substance to a Superfund site is potentially liable for the cost of the entire cleanup.

In practice, EPA sometimes has used the liability system to pursue only a small subset of the potentially responsible parties. These parties then usually try to recover their costs from others who contributed to the contamination at the site. In some of the most egregious cases, companies that have been stuck with the cleanup bill have sued hundreds of smaller parties that had little to do with contamination of the site. Examples of smaller entities that have been sued for contribution include flower shops, two- table pizza parlors -- even the local Elks club.

The bill maintains the "polluter pays" principle but fundamentally revises the manner in which liability among responsible parties is apportioned. It does so in several ways. First, it exempts parties that contributed small quantities of hazardous substances and caps the liability of others who had little to do with contamination of the site or have a limited ability to pay. It also allows small businesses and small contributors to settle their liability quickly.

Second, the bill establishes a new, out-of-court allocation system for use at certain sites. This system will offer parties a way to resolve their liability quickly and fairly without litigation. All of the potentially responsible parties associated with a site will be brought together early in the process and a neutral allocator will assign shares of responsibility based on the available information. All pending response costs litigation regarding the site will be stayed until the allocation process is complete.

The bill also authorizes the payment at certain sites of an "orphan share" from the Superfund. The orphan share will cover the liability of any liable party that can be identified but is either defunct or qualifies for a statutory

exemption from liability. The orphan share will also cover the difference between the full amount of liability of certain parties under current law and the reduced liability under new liability caps added by this bill.

Additionally, the bill includes provisions to protect lenders and trustees from Superfund liability under certain circumstances. These provisions will ameliorate the potential chilling effect on the development of land that can arise from fear of Superfund liability.

Finally, the bill establishes a new Environmental Insurance Resolution Fund to resolve disputes between insurance companies and their policyholders over Superfund liability. About $400 million is spent every year on this kind of litigation by insurers alone -- representing over 80 percent of insurance company Superfund costs expended to date. This fund is designed to significantly reduce the transaction costs and protracted litigation associated with Superfund.

Speeding up Cleanups

Remedy selection is the process by which EPA decides: 1) how clean is clean; and 2) which cleanup technology to use. The bill makes several significant changes to the current remedy selection process to improve cost effectiveness, accelerate the pace of cleanups, and ensure protection of human health and the environment.

The bill provides greater clarity and certainty by establishing a national goal for all Superfund cleanups. The bill also includes reforms that will standardize the way EPA uses risk assessment when making cleanup decisions.

A significant cost saving measure of the bill is the authority to consider the reasonably anticipated future uses of the land as part of the cleanup decision. This change will allow Superfund remedies to be consistent with the projected uses of the land, thereby cutting costs while maintaining protection.

The bill also significantly reforms the current policy for addressing contaminated ground water. Ground water contamination occurs at approximately 85 percent of all Superfund sites. According to a study recently issued by the National Research Council, it is technically impracticable for many of these sites to achieve drinking water standards with currently available

technologies. The bill recognizes this current state of affairs and directs the President to contain in place any contaminated ground water that is found to be impracticable to clean up to drinking water standards. The bill also requires EPA to establish a fund using premiums assessed on the parties responsible for the ground water contamination at these sites to develop the technologies needed to address this problem.

Other changes in the remedy selection provisions of the bill will simplify the way that State and Federal standards from other laws are applied to Superfund cleanups and clarify the preference for the use of treatment remedies.

TITLE BY TITLE SUMMARY

The purpose of the bill is to reauthorize CERCLA for a period of five years and to make major improvements in the Superfund program. The bill is designed to speed the pace and improve the quality of cleanups, reduce transaction and cleanup costs, provide fairness in the allocation of liability, and greatly expand public participation in the cleanup process.

Title I increases the participatory role of communities in the cleanup process by establishing community working groups at individual Superfund sites, expanding the Technical Assistance Grants available under current law, and authorizing Citizen Information and Access Offices in each State to provide information dissemination and public outreach services to affected communities. The title also requires EPA to prepare an environmental justice study, which will analyze and provide comparative information regarding the population, race, ethnicity, and income characteristics of communities affected by Superfund facilities.

Title II establishes the process by which States may be delegated the authority to conduct Superfund response actions. EPA is required to establish by regulation the qualifications a State must demonstrate in order to be delegated the Superfund program, including enforcement authority. Qualified States will enter into contracts or cooperative agreements with EPA to perform such pre-remedial activities such as preliminary assessments and site investigations and other response activities such as remedy selection.

Title III requires EPA to establish a program to assist States in creating or expanding voluntary response programs. The purpose of these programs is to increase the pace of cleanup at contaminated sites that will never be included on the NPL and return these sites to productive economic use.

Title IV establishes a new cost allocation procedure by which potentially responsible parties may resolve their Superfund liabilities, thereby reducing the litigation and transaction costs associated with the Superfund program. Under the new system, allocations of liability will be performed by a neutral third party at all non-Federally owned Superfund facilities involving two or more potentially responsible parties and which meet other criteria set out in the bill. All "orphan shares" (costs traced to defunct or non-viable parties) at facilities where allocations are required will be paid by the Trust Fund. In addition, the title contains exemptions from liability for de micromis (truly tiny) contributors of hazardous substances to Superfund facilities, expedited settlement procedures for de minimis, municipal and small business parties, limitations on liability for generators and transporters of municipal solid waste, and provisions protecting lenders and trustees from liability under certain circumstances.

Title V makes significant changes to the current remedy selection process. To improve the protectiveness, cost effectiveness, and speed of cleanups, the title sets a national goal for protecting human health and the environment and requires the development of a national risk protocol. In addition, the title limits the extent to which other Federal and State laws may dictate cleanup levels, clarifies the role of site-specific risk assessment in Superfund cleanups, authorizes cleanup levels for ground water that are less stringent than drinking water standards under certain circumstances, replaces the current generic preference for treatment (rather than containment) remedies with a preference for treatment that is focused on "hot spots", and emphasizes the consideration of future land uses early in the remedy selection process.

Title VI makes miscellaneous amendments to CERCLA, and Title VII sets out the bill's authorizations of appropriations.

Title VIII establishes a new fund, financed solely by fees on the insurance industry, which will make offers to settle insurance coverage disputes between insurance companies and parties they insured who are potentially responsible parties at Superfund facilities. The new fund will be administered by a Board

which consists of the Administrator of EPA, the Attorney General, and five public members appointed by the President and including two insurer and two PRP representatives. Like the new allocation system established under Title IV, this provision will significantly reduce the protracted litigation between insurers and PRPs that has plagued the Superfund program.

Title IX makes amendments to the Internal Revenue Code of 1986.

SUPPORT FOR THE BILL

As of early August, the following groups have indicated their support of improvements and added fairness embodied in the Superfund Reform Act of 1994:

Aetna Life and Casualty
AgriBank
Allied Signal Inc.
American Automobile Manufacturers Association
American Bankers Association
American Baptist Foundation
American Bible Society
American Communities for Cleanup Equity
American Council on Gift Annuities
American Insurance Association
American International Group
American Land Title Association
American Leprosy Missions, Inc.
American Planning Association
American Public Works Association
Amoco Corporation
Andrews University
ARCO
Ashland Oil, Inc.
Associated Builders & Contractors
Association of American Railroads
AT&T
BancOne
Bank of America

The Bankers Roundtable
Bankers Trust Company
Baptist Foundation of Texas
Barnett Banks, Inc.
The Boeing Company
B P America, Inc.
Browning-Ferris Industries
California Bankers Association
Chemical Manufacturers Association
Chemical Specialties Manufacturers Association
Chevron Corporation
Childrens Medical Foundation of Texas
Chrysler Corporation
The Chubb Corporation
Ciba Geigy
Clean Sites
Commission on Development, United Church of Christ
The Dow Chemical Company
DuPont
ELCA Foundation, Evangelical Lutheran Church of America
Environmental Capital Corporation
Environmental Defense Fund
Equipment Leasing Association
Farm Credit Bank
Farm Credit Bank of Baltimore
Farm Credit Council
Financial Commissioner, State of Montana
First Chicago Corporation
FMC Corporation
General Board of Discipleship, United Methodist Church
General Conference of 7th Day Adventists
General Motors
Good Shepard Foundation
Hercules Incorporated
Hummelstein Iron & Metal, Inc.
Independent Bankers Association of America
Institute of Scrap Recycling Industries
Lloyd's of London

Loma Linda University
Ludy Bible Institute
Massachusetts Mutual Life Insurance Co.
The Mennonite Foundation
Monsanto Company
Mortgage Bankers Association
Mt. Holyoke College
The Municipal Waste Management Association
The National Association of Counties
National Association of Surety Bond Producers
National Association of Towns and Townships
National Committee on Planned Giving
National Federation of Independent Business
The National Paint and Coatings Association
National Realty Committee
National School Boards Association
Natural Resources Defense Council
New Butte Mining, Plc
Northwestern Univeristy
Olin
Printing Industries of America
Rohm and Haas Company
Salvation Army
Savings & Community Bankers of America
Sierra Club
Smith College
Sparten Iron & Metal Corporation
Trail Chemical Corporation
Union Pacific Corporation
The United States Conference of Mayors
United Way of America
WMX Technologies

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What are the problems with Superfund and how does S.1834 solve them?

PROBLEM	S. 1834's SOLUTION
How Clean Is Clean?	
Inconsistent standards: Individual project managers require attainment of different clean up levels, and there is little explanation of why one site is expected to be cleaner than another.	Each site shall seek to attain the same cleanup goal, with clearly explained variations allowed to accommodate problems based on technology and unreasonable cost.
Unreasonable risk assumptions: Clean-up levels are set assuming the worst possible case in terms of a site's threat to human health and the environment even when the real facts warrant a less conservative assumption.	Clean-up levels will be established by using a new national risk protocol that: • Uses actual, reliable site data. • Requires that assumptions and risk assessment be realistic. • Still ensures that sensitive populations found at a particular site are not ignored.
Land Use: All sites are expected to be cleaned up to levels children can play on, even when a particular site will never be used for such sensitive purposes.	Different clean-up levels are set by formula depending on how land really will be used now and in the future, and the remedy is designed with that land use in mind.
ARARs: The standards for cleanup (ARARs) are too complex, borrowed from programs that have nothing to do with old disposal sites.	ARARs are largely eliminated. Instead, only applicable Federal and State requirements are used and their applicability to cleanup situations must be subject to public comment.
Groundwater: The goal of ground water restoration is beyond current technology.	A new remedy selection process assures preservation of usable groundwater but also allows for site-specific determinations where less rigorous cleanups make more sense.

Bad science: EPA's risk assessments aren't consistent and aren't updated to reflect new science.

The new risk protocol will be standardized and updated periodically.

Treatment mandate: Broad preferences for permanence and treatment can lead to "gold plated" remedies.

Treatment is preferred only for "hot spots," not the entire site. Sound engineering judgment controls selection of remedy.

Cost: Cleanup costs are frequently ignored when clean-up technologies are chosen, even though the law says they must be cost effective.

Cost is put on an equal basis with other factors in remedy selection. Remedies must have "reasonable" costs, not just be cost-effective.

Standard remedies: The remedy selection process at each site "reinvents the wheel" even if the problem and solution are fairly obvious.

EPA is to develop and use standard generic remedies for common types of sites, and implement them with streamlined procedures.

No further action: The system doesn't recognize that removal, the first thing done at a site to take care of immediate threats, sometimes solves the whole problem.

The scope of removals is doubled, and it is clear that removals can serve as the total response at a site if they meet protective standards.

Who pays how much?

Disproportionate liability: Joint and several liability means that "deep pockets" are charged an unfair amount.

An allocation of responsibility at each site with mandatory funding of the orphan share by the Superfund means each party pays its fair share.

Litigation costs: The only way a PRP can get "rough justice" is to sue everyone involved in the case, thus lining the pockets of lawyers.

EPA is obligated to find all liable parties, and an informal allocation replaces protracted third-party litigation to establish fair share. EPA can reject the allocation only under extraordinary circumstances.

Litigation delay: Cleanup is slowed while PRPs go through tiers of contribution litigation in search of adequate funding.

There are mandated deadlines for determining liability in a single, comprehensive proceeding. The cleanup process proceeds on a separate track. Contribution suits are eliminated for settlers.

PRP-led cleanup: Any PRP who agrees to perform remediation has to sue other PRPs to get reimbursement of expenses above its fair share.

EPA guarantees reimbursement to the PRP who undertakes cleanup, thus assuring that the cost savings and efficiencies of private- sector-conducted cleanups continue.

Recalcitrants: Parties who "lie in the weeds" usually get off the hook.

EPA is obligated to sue recalcitrants in order to replenish the fund.

Insurance claims: More money is spent litigating insurance coverage than is used to reimburse PRPs for the cleanup covered by their insurance contracts.

A highly streamlined dispute resolution process is established to resolve insurance claims without litigation.

Administrative costs: Government oversight costs are sometimes as much as the cost of the response action.

Government oversight costs are capped at no more than 10% of response costs.

What happens to small businesses?

Ability to pay: Small companies have been driven out of business by Superfund because they simply cannot pay the bills.

EPA is required to consider a small business's ability to pay (including timed payments) and still maintain basic business operations. A small business ombudsman will help assure small businesses are aware of their new rights.

"Truly tiny" parties: Flower shops and pizza parlors who sent one drum of waste to a site are extorted into disproportionate payment because of joint and several liability.

Small businesses who only sent municipal waste or who sent less than one drum or a hundred pounds of non-municipal waste are exempt from liability.

De minimis: EPA rarely uses its *de minimis* settlement authority to help small businesses and other small contributors negotiate out of litigation.

EPA's obligation to enter into *de minimis* settlements is strengthened and streamlined; there are clear standards to get small contributors settled out early in the process and at a level reflecting their ability to pay.

Indefinite liability: Small businesses can lose their ability to get financing because of the uncertainty of joint and several liability and the length of time it takes to get liability resolved.

Joint and several liability is replaced by fair share liability, so disproportionate claims are not threatened. If EPA fails to meet tight settlement deadlines, it loses the ability to charge a settlement premium -- or to recover altogether.

PRP disputes: Big and small business are at odds because where one company gets a break, the other party picks up a share.

If small businesses demonstrate inability to pay, the orphan share picks up responsibility.

Are the concerns of local governments addressed?

Trash generators & haulers: Municipalities face vast potential liabilities simply for sending ordinary trash to a landfill. Large litigation fees are incurred proving at each site how little hazardous substance appears in garbage.

Recognizing that ordinary trash contains *de minimis* amounts of hazardous substances, municipal waste generators and transporters' share of liability is capped at no more than 10% of total response cost. If the share of these parties (both municipalities and private parties who produce and transport municipal waste) would have been higher without the 10% cap, any overage is paid for as an orphan share.

Municipal owners: Municipalities who are Superfund site owners or operators may be asked to pay so much to remediate they are unable to continue vital public services.

If a municipality can demonstrate inability to pay according to fair and consistent standards, any additional needed funds will come from the orphan share. Municipalities are encouraged to make use of in-kind services to make up their share.

Small municipalities: Very small municipalities simply cannot pay their share of Superfund at sites they owned or operated.

Municipalities with under 100,000 people have owner/operator liability capped at 10 percent, with the overage going to the orphan share.

Do lenders have reason to fear issuing loans?

Management guidelines: Lenders have no guidelines on how to avoid Superfund liability arising simply because of a business loan.

The law is clear that the financial community becomes enmeshed in Superfund only where they actually manage the site.

Redevelopment barriers: Business avoids redeveloping sites in urban areas because of fear of Superfund liability.

Bona fide prospective purchasers (and there are clear definitions for this) are not liable so long as they allow cleanup to progress.

How is the role of the community impacted?

Sufficient technical support: Communities rarely have sufficient information and technical advice to fully and fairly participate in evaluating potential health threats and remedial options.

Constraints on availability of technical assistance grants are eliminated, and Community Work Group and Community Information Access Office supports are mandated to assure that each community will receive the technical and scientific information necessary to make sound judgments.

Last-minute objections: Citizens are excluded from the remedial process except for formal comment on the Record of Decision and haphazard outreach efforts. Their only meaningful input is their ability to object, at the end of the process.

Local citizens and PRPs work directly together throughout the investigation and remediation process to gather information and share views on how land will be used and what remedial measures will be reliable at the site.

Environmental justice concerns: The current program is so complex that different communities receive radically different levels of cleanup, and there is no reporting mechanism to assure that these disparities do not work to the disadvantage of minority and poor communities.

The goal of Superfund is revised to assure that all communities receive an equivalent level of protection. Routine reporting obligations will assure that the extent of cleanup and the time it takes to get it done are equivalent among communities.

Is voluntary cleanup encouraged or discouraged?

EPA interference: If a private party decides to voluntarily clean up early in order to avoid becoming enmeshed in Superfund, it has no assurance EPA won't intervene at any point and start the Superfund process.	States are given federal funding to initiate voluntary cleanup programs, and EPA action is stayed. Even proposed NPL-calibre sites can undergo state-approved cleanups.
Superfund red tape: Even low priority sites have to follow every procedural detail.	States have maximum authority to develop their own programs tailored to local concerns.
Finality: After a voluntary cleanup is completed, there is no official government acknowledgement of this action.	The state will provide certifications that voluntary cleanups have been conducted under work plans approved by the state, and the state will certify completion of construction. If further cleanup eventually is needed, earlier remedial measures must be taken into account.

Will the private sector invest in developing better technologies?

Risk of failure: Few companies are willing to invest in new and better technologies because PRPs are reluctant to use anything new: if the new technology fails, the PRP has to pay for two cleanups.	Where an innovative technology fails, the Superfund will subsidize the PRP for 50% of the costs of obtaining an effective final remedy.
Clearer market definition: Because clean-up standards are uncertain, treatment obligations are broad and unevenly handled -- and everyone expects that a reauthorized Superfund will change the rules of the game, it is extremely risky to invest now in better technologies.	S.1834 makes clean-up levels clearer, narrows and makes more predictable treatment obligations, recognizes the need to develop new ground water technologies, and -- if passed this year -- provides strong market potential for better and cheaper technologies.

Conclusion

S. 1834, like its substantially similar House counterpart, H.R. 3800, makes Superfund faster, fairer, more efficient, more uniformally protective, cheaper and better tailored to best available science and technology. If passed this year, it provides critically needed reform to an important but deeply flawed program.

PREPARED STATEMENT OF ALICIA H. MUNNELL

Mr. Chairman and Members of the Committee: I appreciate the opportunity to appear before you today. Before Assistant Secretary Samuels discusses the specific funding proposals that are the subject of today's hearings, we thought that some background information on the broader subject of Superfund reform might be useful. As you know, Superfund—the Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA)—was enacted in 1980 in response to public outcry over Love Canal, Valley of the Drums, and other environmental disasters. The original vision was that the program would involve relatively inexpensive clean-ups of a few hundred sites. Actual events have turned out to be quite different. Currently, EPA has roughly 1,300 sites on the national priority list. Most observers envision an eventual number of at least 3,000 and cost estimates are running as high as $150 to $300 billion.

Major problems with the program are that fewer than 20 percent of the identified priority sites have been cleaned-up to date and for every dollar spent, more than 25 percent goes to lawyers and transaction costs. The incentives in the system are all wrong. They lead to pressure for Cadillac-type clean-ups and endless wrangling over who's going to pay and how much.

The current system is in desperate need of reform. Under Superfund, liability for the costs of cleaning up hazardous substances is strict, joint and several, and retroactive. While this scheme provides great benefits for the efficient operation of EPA's cleanup program, there is no question that it also spawns a tremendous amount of litigation. This litigation is so extensive and costly that the President has twice called for a solution to the problem, most recently in his State of the Union Address this year.

Under current law, a settlement by the Environmental Protection Agency (EPA) with a potentially responsible party (PRP) at a site with multiple PRPs (either voluntarily or through litigation) results in those liable parties seeking to distribute the costs of clean up by initiating contribution litigation against other PRPs. Since insurance companies generally have taken the position that their policies do not cover Superfund response costs, the PRPs frequently must sue their insurance companies in order to try to recover their costs. This litigation among PRPs and among PRPs and their insurance companies has proven to be extensive and very costly and is a major impetus for many of the Administration's proposals for Superfund reform.

One of the Administration's major objectives in Superfund reform is to eliminate—or at least drastically reduce—all of these lawsuits, without eliminating the beneficial effect of joint and several liability, specifically the ability of EPA to order PRPs to begin cleanups. These lawsuits impose substantial transactions costs on policyholders and insurance companies. The Administration has addressed lawsuits among PRPs by proposing a more reasonable mechanism for allocating costs among parties. The bill provides for early settlement for small contributors, generators and transporters of municipal solid waste, and parties with limited ability to pay. Under these provisions, most small businesses will be out early and without great expense.

The bill also establishes a process for allocating shares of all remaining PRPs at a site in a single proceeding. In this process, the remaining PRPs will sit at a table, and a mediator will allocate liability based on factors such as the volume and toxicity of their waste. Parties who accept the allocation (1) will be protected from suits by other PRPs; (2) benefit from EPA's funding of orphan shares—shares established in either the early settlement process or attributable to insolvent parties; and (3), for a fee, will be protected from future liability for remedy failure or some undiscovered harm. Under these provisions, the large businesses that run most of the clean-ups will be treated much more fairly.

To address lawsuits by policyholders against insurance companies, the Administration has proposed establishing the Environmental Insurance Resolution Fund. The Resolution Fund, detailed in Title VIII of the reauthorization bill, is a compromise proposal developed by policyholders and insurers and, as such, it represents the framework by which to solve a particularly vexing problem. The Administration brought the parties together, worked with them to develop the principles underlying the proposal and resolve differences in the details, and drafted initial legislative language that was included in the Administration's original Superfund-reform proposal. Since the Administration presented this proposal in early February, representatives of insurers and policyholders have continued to work to refine the mechanics of the Resolution Fund proposal, and it is this revised proposal that is included in the bill that you are considering.

In addition, the Treasury Department has continued to examine the administrative structure of the Resolution Fund to ensure that there is appropriate oversight and control over the Fund's operations. We believe that the Resolution Fund meets

the needs of all stakeholders, is consistent with the Administration's policies, and can be implemented and administered by the Administration.

The Resolution Fund is designed to dramatically reduce lawsuits among policyholders and insurers arising out of Superfund liability through a two-step process. First, the proposal would stay all Superfund insurance litigation. Second, the Resolution Fund will make to each eligible policyholder a one-time comprehensive offer to resolve all pending and future claims of that policyholder against its insurers arising under the Superfund law for all eligible costs of the policyholder.

The one-time offer is designed to avoid adverse selection by policyholders, whereby they would accept offers for sites where their probability of litigation success was low and elect to sue their insurers where their probability of litigation success was high. If policyholders could make a separate choice at each site, insurers would end up paying fees and assessments to the Resolution Fund, and also paying policyholders in litigation. To minimize this problem, the offer made by the Resolution Fund to a policyholder would be for all the eligible costs of a policyholder at all of its eligible sites.

- To be eligible to receive an offer from the Resolution Fund, a policyholder must demonstrate that it purchased the types of insurance coverage that give rise to claims based on Superfund liability. (In the event that a policyholder can submit only partial documentation, the insurance companies that it names will make a good faith attempt to provide copies of the relevant policies.)
- An eligible site is (1) any site placed on the National Priorities List (NPL) and (2) any site that is the subject of a removal under Superfund.
- Eligible costs are those incurred by a policyholder, at any site that accepted waste prior to 1986, for response or removal actions, natural resource damages, and activities that would be covered by a duty-to-defend clause in an insurance contract.
- The limits of coverage by the Fund will be determined by summing up all of the liability limits contained in the insurance policies presented as proof of eligibility, and subtracting the sum of all deductibles and self-insurance retentions applicable to those policies.

The offer made by the Resolution Fund will be for a percentage of the policyholder's eligible costs at all eligible sites. To arrive at this offer, the Fund will take into account both the geographic location of the sites and any litigation venues that the policyholder has established. Each site and litigation venue will be assigned an offer percentage, according to which of three groups of states it belongs. These percentages will then be weighted together—with varying degrees of complexity depending on the circumstances of the policyholder—to arrive at a single percentage offer that will apply to all of the policyholder's sites. Finally, only for claims presented to the Fund for "owned-property" sites, the compensation from the Fund will be reduced by 30 percent.

The percentages contained in the proposal are necessarily subjective, reflecting levels that take into account both the perceived probability of litigation success and the inducements considered necessary to persuade policyholders to accept offers made by the Resolution Fund. (The adjustment for compensation for costs incurred by policyholders at "owned-property sites" is an example of the attempts made to reflect reality in the plan for the EIRF.) What is most important, however, is to be sure that the percentage offers made by the Resolution Fund are sufficient to obtain maximum policyholder participation in the program, while at the same time minimizing windfalls to policyholders that have virtually no probability of succeeding in litigation against their insurers. Without this balance, the Resolution Fund would not succeed.

Participation in the Resolution Fund by a policyholder is entirely voluntary; a policyholder may either accept or decline the offer made by the Resolution Fund. If a policyholder accepts the offer made by the Fund, it must agree to stay or dismiss all pending litigation against its insurer for claims arising under Superfund, and must waive future claims against its insurers for pre-1986 costs. The policyholder will then submit documentation of its eligible costs to the Resolution Fund for payment. If the eligible costs were incurred before the policyholder accepted the offer, those costs will be paid by the Resolution Fund in equal installments over 10 years. If the eligible costs are incurred after the policyholder accepted the offer, they will be paid by the Resolution Fund as they are submitted in the context of an ongoing cleanup. If, during the first ten years after enactment, the Fund does not have sufficient funds to pay these costs as they are presented, the shortfall can be amortized over five years.

If a policyholder declines the offer made by the Resolution Fund, only then may it pursue litigation against its insurers. But, if the policyholder is not successful in that litigation, it may not revive the offer from the Resolution Fund. If the policy-

holder is successful in the litigation, the Resolution Fund will reimburse the insurer for its liability, up to the amount of the offer made by the Resolution Fund to the policyholder. In addition, if the policyholder is successful in the litigation, but obtains a judgment that is less favorable than the offer made by the Resolution Fund, the Resolution Fund has the discretion to reimburse the insurer for all or some of its litigation costs.

The terms for the Fund that I have described are not the same as those contained in the Administration's original bill. The changes reflect substantial additional negotiations among interested parties, and restructure the necessary compromises much more efficiently. From my point of view, the most substantial change in the program was its transformation from a five-year authorization for resolution payments to one in which the Fund will make offers of resolution for ten years, and honor the commitments inherent in those offers until they are fully discharged. These changes obviously expand the scope of the proposal, but they also greatly reduce the uncertainty for both insurers and policyholders. Once the Fund is up and running and achieves whatever participation level is necessary for its continuation, it will proceed to resolve the vast proportion of claims.

To conclude, no one is happy with every aspect of the proposed Superfund Reauthorization Bill. No one wants to have to invest scarce resources to clean up problems left over from the past, but it has to be done, not only because Superfund sites are a health hazard, but because they are also an economic hazard. These sites need to be cleaned up and redeveloped so that they can add to the well-being of the communities in which they are located, not subtract. We have spent an enormous amount of time and effort trying to reach appropriate compromises on difficult and delicate issues. The time is right for the passage of Superfund reauthorization. The proposed bill makes great strides in addressing the shortcomings of the current system. That is why the Administration is happy to support it and, even more important, why it has received such widespread support from those with an important stake in Superfund reform.

Prepared Statement of Michael Murphy

Mr. Chairman and Members of the Committee:

I am pleased to present testimony to the Senate Finance Committee on this important legislation. My name is Michael Murphy. I am counsel to the Chairman of American International Group, Inc. (AIG). AIG is one of the largest commercial property and casualty insurance companies doing business in the United States which is affected by the proposed Superfund tax.

BACKGROUND

Agreement on the funding provisions of the Environmental Insurance Resolution Fund (EIRF) in the Superfund Reform Act represents a highly contested and very delicately balanced compromise.

The original Administration proposal constituted a compromise for AIG but was acceptable because it represented an attempt to raise revenues for the EIRF from the parties which would be released from liability. In early 1994, the Administration proposed a funding formula for insurers that raised 70% of the funds through a retrospective formula applied to a pre-1986 premium base for specific court-contested, environmental lines of business. The remaining 30% of EIRF funding was designed to come from a prospective assessment of certain commercial lines of insurance.

It was the Administration's view at that time, and AIG concurred, that the same insurers which issued these pre-1986 policies, and financially benefited from premium collections, were also the companies which stood to benefit most from the release from legal liability under the bill's provisions. The formula caused those insurers which financially benefited from originally collecting premiums, and which would be released from the greatest liability, to pay for such benefits. This is the traditional, time-tested principle by which all insurance settlement funds have been organized and operated.

AIG originally opposed the Administration's "70–30" proposal because it failed to achieve two major objectives: (1) the bill did not relieve joint and several, retroactive liability and (2) the bill did not include a broad-based assessment for creation of an EIRF which, in turn, would be used to clean up Superfund sites rather than settle past claims as the EIRF, which you are about to consider does.

It became apparent that the Congress would not support relief from joint and several liability nor a broad-based clean-up tax. For that reason, AIG reluctantly supported the Administration's "70–30" EIRF funding compromise because the proposal did relieve some joint and several liability and substantially followed traditional

trust fund settlement concepts. In the Administration compromise, insurers which financially benefited from release of legal liability on their environmental related policies issued prior to 1986, would fund the EIRF in exchange for release from legal liability.

After the Administration's "70–30" compromise was rejected for consideration by the House Ways and Means Committee, AIG, along with other commercial insurers, participated in difficult negotiations with the Administration which produced the very delicate and intensely negotiated compromise before you today. AIG, along with other insurance groups, collectively representing more than 50% of the premium subject to the taxes being considered, and the Administration, have agreed to support the EIRF funding mechanism, and the overall bill itself, on condition that no part of the funding mechanism before you today be changed in a meaningful way.

EIRF FINANCING PROPOSAL

The compromise that eventually was approved by the Ways and Means Committee is intended to raise $810 million per year for a maximum of 10 years, or $8.1 billion. The Premium based fee is divided prospectively and retrospectively and applies to direct insurance premiums and reinsurance premiums. The retrospective element is assessed premiums against collected on Commercial Multiperil and Other Liability lines of business during the 1968–1985 base period, while the prospective element applies to a premium base of certain lines of identified commercial insurance premiums collected after the bill is enacted.

Other parts of the funding include special assessments, capped at $85 million per year, or $810 million over 10 years, based on limits of liability applicable to insurance policies used in the EIRF settlements after appropriate deduction for reinsurance limits originally placed under such contracts. In addition, a special assessment is applied to the reinsurance base which is intended to spread the accounting for the tax over a 10-year period.

In total, 23.2% of the funding, or $188 million per year, is to be raised from a retrospective tax on reinsurance premiums while the direct insurance base covers 76.8% of the tax. The domestic insurance companies absorb at least 25% of the reinsurance liability since they write at least 25% of the reinsurance premium.

During the first 4 years, 70% of the funding would be assessed on a retrospective basis and 30% prospective, while in the final 6 years, 35% would be retrospective and 65% prospective. In the 9th year, the Treasury is directed to conduct a study and submit to Congress a recommended method for future funding of the EIRF beyond 2005. The tax title of the bill (Title 9) sunsets December 31, 2005. It is understood that the Treasury is not to draw any inference in its study from the prospective-retrospective allocations in the current proposal.

Because of its total commitment to the retrospective part of the agreement, AIG would consider any change in the retrospective/prospective proportions under the current proposal as a "meaningful change" in the compromise agreement which would mandate that the Administration, along with other parties to the agreement, support the removal of the entire EIRF funding mechanism as well as the EIRF from the proposed legislation.

RETROSPECTIVE EIRF ASSESSMENTS NOT A RETROACTIVE TAX

The retrospective elements of this compromise do not create retroactive tax liability in the insurance tax as suggested by some members of Congress. The retrospective element is not truly a tax at all, but a reasonable formula for the assessment of those insurers who benefit from the release of their legally binding contractual liabilities for the period which the EIRF covers.

AIG continues to hold the retrospective elements of the compromise as most important. To have done otherwise, would suggest that the insurance industry can come to Congress seeking relief of its legally contracted, binding insurance obligations (the core reason for its existence within society), and expect that insurers other than those who incurred the liability would pay for such relief

The EIRF settles claims on commercial general liability and commercial multiperil insurance policies issued prior to 1986. The retrospective tax base applies to premiums collected on these same lines of business for the 1968–85 base period. The retrospective tax is collected over a four year period from 1995 through 1998. The assessments collected are not included in the Treasury's general revenues, but are specifically earmarked for settlement of costs with potentially responsible parties (PRPs) and others. The entire administrative costs under the EIRF are paid from assessments and user fees.

What other tax has been considered by Congress that also has the effect of relieving the payer from legal liability and pays for its own administrative handling costs?

REINSURANCE ASSESSMENT IS MORE THAN FAIR

The reinsurance retrospective assessment is proper, fair and relieves far more proportionate liability than the 23.2% proportionate assessment represents. The reinsurer's segment of the tax has been allocated based on similar principles of retrospective responsibility. The reinsurers will incur an assessment of 23.2% or $188 million per year for 10 years in exchange for relief from their liability under pre-1986 contracts. If a portion of this assessment were applied prospectively, market conditions would suggest the probability of a portion of the tax being absorbed by the direct writing insurers.

It is AIG's view that reinsurance generally represents a much smaller percentage of total property and casualty premiums and surplus than their potential liability for Superfund claims. Domestic reinsurers accept that somewhere between 21% and 23% of proportionate tax liability for funding the EIRF accrues to reinsurers, based on analysis of the reinsurer's proportionate share of the industry premiums, regardless of where the liability falls.

(See Exhibit 1 which demonstrates that the premium base for the 1968–1985 base year was 22.6% of total industry premiums on the relevant lines of business.)

The compromise funding formula assigns 23.2% of the share of funding the EIRF to reinsurers. AIG maintains that "fair share" should be measured on the basis of proportionate premiums collected by each sector and by proportionate liability being relieved by the EIRF. According to *Best's Aggregates and Averages,* approximately 50% of the court contested lines of General Liability and Commercial Multiperil loss reserves pertaining to the relevant accident years 1985 and prior are reinsured. (See Exhibit 2) While these figures are presented on a gross basis and contain insurance and reinsurance segments unrelated to environmental claims, they are one of the few public statistics available to demonstrate the structure of the reinsurance in place containing the relevant lines subject to the tax.

This evidence would indicate that the 23.2% share of the tax reinsurers are being asked to fund is low relative to the share of the losses they are otherwise likely to incur in the future. Looking at the annual statements of 25 of the largest direct companies, per *Best's Reproduction of Annual Statements,* these 25 companies are ceding an average of 42% of their General Liability and Commercial Multiperil loss reserves for accident years 1985 and prior, further supporting the likelihood of future liability for the reinsurers above their 23.2% of the tax. (See Exhibit 2)

Additionally, Best's Aggregates and Averages shows that industry Paid Losses since 1990, pertaining to accident years 1985 and prior, have had over 50% of the gross amounts ceded to reinsurers, thus following the same trend as the reserves. (See Exhibit 3)

Again, while these public statistics contain other liabilities unrelated to environmental claims, they generally reflect the structure of the reinsurance when measuring what portion of the potential extensive environmental liabilities will fall on the reinsurance industry. In addition, industry studies on environmental liability have indicated that the reinsurer's proportional share could be as high as 50%.

It is still very early in measuring exactly where proportionate liability for Superfund claims will fall, but AIG's own experience on the limited amount of direct excess environmental claims settled indicate that in excess of 70% of such amount has been paid by reinsurers. This compares favorably with AIG's reinsurance structure as presented in the Exhibit demonstrating the reinsurance structure for the twenty-five largest companies averages 40% reinsurance. The 25% share therefore appears to be a favorable ratio for reinsurers based on the actual losses being ceded to reinsurers for all General Liability and Commercial Multiperil losses.

In establishing the corresponding premium analysis for both direct insurance and reinsurance, there is no evidence to show what portion of the direct insurance or reinsurance will fail to pay the tax because of insolvencies or because of non compliance, particularly among foreign insurers and reinsurers.

In establishing the premium tax percentages, the direct insurers recognize that more than 234 domestic direct-writing insurance companies have failed between 1969–1988 and that the premium levies these companies would have paid under the EIRF are not collectible and must be absorbed by the existing healthy direct writing companies. The existing state organized insolvency guarantee funds cannot be viewed as an excuse for direct writers, affected by the EIRF, to absorb these costs since the base to which the EIRF fee is applied is limited to certain narrower commercial lines of business, while the guarantee fund payments for insolvency are spread over a much broader base, which includes the entire direct writing industry, including personal lines insurers which pay very little of the EIRF assessment.

Also, under the Administration proposal, US direct writers are required to absorb unknown amounts, which may result in very substantial additional taxes, which

will not be paid by those foreign direct writing insurers which fail to comply with the tax or have gone insolvent after writing these lines of business in the 1968—1985 base period. While the amount of premiums and tax liability attributable to these failed foreign direct writers and foreign direct non compilers is not known, a London market critic estimated that as much as 50% of Lloyds of London's potential liability, attributable to its various syndicates for pollution claims, may be from writing direct insurance from London. While no foreign insurer or reinsurer presented any premium statistics, expected failure statistics or potential liability statistics for foreign direct insurers, their tax liability under the EIRF will be absorbed by the domestic direct writers. Similarly, no statistics were presented as potential failure for foreign reinsurers or foreign non-compliance. Moreover, the domestic direct writers already bear 25% of the total risks the domestic reinsurers bear, as it represents the former's own share of the reinsurance premium. However, in light of the compromise reached with the insurers, AIG is satisfied with the Administration's negotiated settlement.

TECHNICAL ISSUES

Caps

It is imperative that the EIRF funding be clearly separated into 5 segments, each with a cap on the amount of funds to be collected each year. These categories and corresponding caps were separately negotiated and agreed to by the Administration and the insurance industry. The following table shows the categories and corresponding fee caps which we need to be included in the bill as absolute amounts of liability. This assessment process is not in the nature of an income tax but merely a funding of an insurance settlement trust fund where the commitment by the insurers must be known.

INSURER CATEGORY:	PROSPECTIVE	RETROSPECTIVE
Direct insurers		
Years through 4	$248mm/year	$374mm/year
Years 5 through 10	$537mm/year	$ 85mm/year*
Reinsurers		
Years 1 through 10	$537mm/year	$188mm/year

(*Separate reconciliation fund payments)

AIG considers the funding caps to be an integral part of the negotiated agreement. If these caps are not established then each group runs the risk of paying for the liability of others if their corresponding applicable rates are not properly established in relation to each other. Since the tax is not meant to be collected from each respective group once the year's targeted amounts are reached, caps are essential to meet this objective.

Separate caps are necessary to avoid collecting excess amounts from direct insurers when determining the amount which should be paid from the prospective base of premium and the amount which should come from the 1968—1985 retrospective base of premium, since different direct insurers and market shares comprise these two groups of insurance underwriters.

The caps to be established for the domestic and foreign elements of reinsurance have not yet been set but must clearly avoid establishing any orphan share that would spill over to the direct insurers.

Failure to establish these separate categories of caps on funding the EIRF would breach the Administration's agreement with the insurers with which it negotiated and would obligate all parties to the agreement to abandon their support of the EIRF.

TECHNICAL ISSUES

Sunset provisions and borrowing authority of the EIRF

The proposal accepted by the House Ways and Means Committee contains a provision which sunsets the EIRF tax after 10 years. In other words, if, after 10 years, the outstanding liabilities or claims against the EIRF exceed remaining undistributed revenues, the Congress may be forced to renew a level of funding for the EIRF and, if so, must then re-examine the funding allocation formula between the prospective and retrospective portions.

We believe that a sunset provision similar to the House version is vital to those insurers supporting the retrospective tax who agreed to work with the Administra-

tion in developing the proposal before you. Contrary to AIG's understanding of the latest agreement with the insurers and reinsurers and the Administration, the Administration has asserted that this new compromise proposal does not sunset the tax at 10 years, and appears to use the retrospective/prospective split as of the tenth year for a perpetual period beyond 10 years.

There is sufficient penalty to the entire insurance industry to force a refunding to the extent EIRF liabilities in year 10 exceed revenues available. If the EIRF were forced to default in year 10 on the payment of claims due to the lack of revenues, all of the coverage-litigation could be revived under the existing bill. The insurance industry will have paid $8.1 billion in taxes and still have to face the litigation the EIRF was intended to resolve. In addition, sufficient pressure would mount from the PRPs to force a refunding after year 10.

The Administration has agreed with the insurers who support the proposal before you to remain neutral as to the division between prospective and retrospective assessments on future funding of unfunded liabilities beyond year 10.

It is imperative that funding of these liabilities be revisited in the most neutral manner possible. A sunset forces all parties to renegotiate the remaining amount of funding necessary, but gives the PRPs the opportunity to restart the litigation at the cost of a wasted $8.1 billion to the insurance industry. This should provide ample incentive for all parties to come to future agreement. AIG cannot accept a funding formula beyond year 10 which would continue the prospective/retrospective ratio in years 5–10 in the current proposal. We are confident the Administration also recognized the sensitivity of the prospective/retrospective allocation by not objecting to the sunset provision as passed by the Ways and Means Committee. If limited EIRF borrowing power is to be added to the mix, it creates one more party—the federal government—which would be applying pressure to have an agreement on new funding in Year 11.

TREASURY AUTHORITY TO EXPAND LINES OF BUSINESS TO WHICH THE EIRF WOULD APPLY

The House bill inadvertently expands Treasury's authority to increase the lines of business to which the prospective tax should apply. Such a power is unintended but if not remedied would give the Treasury direct authority to expand the tax base without legislative consideration.

The original intent of this provision was to give the Treasury power only to continue to apply the prospective tax to the original existing base on lines of premium to which it is intended to apply. Generally, these lines are divided in the State Statutory Insurance Financial filings made by each domestic direct writing insurer. The Treasury's authority should be limited, allowing Treasury to prevent the base of the tax approved by Congress from eroding, but not to expand the base by including additional lines of insurance without prior approval of Congress.

EXHIBIT 1

DIRECT PREMIUMS

+ ASSUMED PREMIUMS
= GROSS PREMIUMS
− CEDED PREMIUMS
= NET PREMIUMS

ENVIRONMENTAL INSURANCE RESOLUTION FUND

FACTS AND ASSUMPTIONS

Facts:

1. Net written premiums of domestic direct insurers were 81.14% of direct written premiums for Other Liability and Commercial Multiple Peril coverages during the years 1968 to 1985 when expressed in 1985 dollars.

2. Domestic insurers net written premiums for Other Liability and Commercial Multi Peril coverages during the years 1968 to 1985 were equal to 91.38% of the total net premiums written by domestic insurers and domestic professional reinsurers for these lines of business in these years.

3. Domestic professional reinsurers wrote 72.2% and domestic direct insurers wrote 27.8% of the net reinsurance premiums written for Other Liability and Commercial Multiple Peril coverages during the years 1968 to 1985.

Assumptions:

1. Foreign direct insurers wrote an additional 5.00% of direct written premiums for Other Liability and Commercial Multiple Peril coverages during the years 1968 to 1985. This direct premium was reinsured at an average of 40%.

REVRIN85

PRIMARY VS. REINSURER SHARE OF U.S. MARKET
(000'S OMITTED)

	DOMESTIC PRIMARY INSUR — WORLDWIDE NET PREM. WRITTEN PER GEN RE			INDUSTRY — U.S. DIRECT PREMIUMS WRITTEN PER BESTS				
	OTHER LIABILITY	COMMERCIAL MULTIPLE PERIL	TOTAL OTHER LIAB & CMP	OTHER LIABILITY	COMMERCIAL MULTIPLE PERIL	TOTAL OTHER LIAB & CMP	DOM. PRIM. PERCENTAGE	REINSURERS PERCENTAGE
1968	1,395,883	888,301	2,284,184	1,496,003	1,028,338	2,524,341		
1969	1,607,464	1,051,817	2,659,281	1,724,013	1,209,533	2,933,546		
1970	1,990,865	1,261,173	3,252,038	2,145,795	1,447,258	3,593,053		
1971	2,267,538	1,583,123	3,850,661	2,398,222	1,776,389	4,174,611		
1972	2,437,904	1,990,521	4,428,425	2,555,556	2,201,220	4,756,776		
1973	2,566,873	2,415,716	4,982,589	2,726,013	2,667,628	5,393,641		
1974	2,795,850	2,729,752	5,525,602	3,023,822	3,087,319	6,111,141		
1975	2,846,058	3,014,481	5,860,539	3,186,267	3,458,652	6,644,919		
1976	3,868,176	3,834,228	7,702,404	4,624,323	4,403,280	9,027,603		
1977	5,251,419	4,711,919	9,963,338	6,593,784	5,387,042	11,980,826		
1978	5,986,962	5,602,383	11,589,345	7,749,744	6,482,316	14,232,060		
1979	6,139,648	6,400,520	12,540,168	8,151,105	7,343,320	15,494,425		
1980	5,956,484	6,599,504	12,555,988	7,917,553	7,663,589	15,581,142		
1981	5,594,089	6,567,694	12,161,783	7,693,363	7,744,896	15,438,259		
1982	5,178,959	6,682,875	11,861,834	7,314,246	7,979,948	15,294,194		
1983	5,147,395	6,932,355	12,079,750	7,412,075	8,292,519	15,704,594		
1984	5,944,259	7,851,174	13,795,433	8,806,196	9,461,856	18,268,052		
1985	10,572,927	11,492,552	22,065,479	15,536,966	13,954,330	29,491,296		
SUB-TOTAL	77,548,753	81,610,088	159,158,841	101,055,046	95,589,433	196,644,479	80.9374%	19.0626%
U.S. PERCENTAGE	97.0825%	98.7102%		100.0000%	100.0000%			
U.S. TOTALS	75,286,268	80,557,481	155,843,749	101,055,046	95,589,433	196,644,479	79.2515%	20.7485%

REVRD85

RATIO OF U.S. TO WORLDWIDE DIRECT PREMIUMS WRITTEN 1984 - 1992
(000'S OMITTED)

	---OTHER LIABILITY---			-------C.M.P.------		
	U.S.	WORLDWIDE	% U.S.	U.S.	WORLDWIDE	% U.S.
1984	8,806,196	9,063,720	97.1587%	9,461,856	9,622,035	98.3353%
1985	15,536,966	16,048,871	96.8103%	13,954,330	14,141,867	98.6739%
1986	24,091,170	24,836,356	96.9996%	18,245,020	18,483,557	98.7095%
1987	24,825,810	25,654,534	96.7697%	19,013,930	19,215,384	98.9516%
1988	23,106,634	23,875,586	96.7793%	19,155,002	19,372,939	98.8750%
1989	22,451,100	23,233,099	96.6341%	18,875,981	19,127,068	98.6873%
1990	22,610,904	23,300,114	97.0420%	19,123,932	19,379,817	98.6796%
1991	21,184,920	21,630,443	97.9403%	18,445,313	18,682,825	98.7287%
1992	21,582,604	22,088,929	97.7078%	18,001,878	18,267,663	98.5451%
TOTAL	184,196,304	189,731,652	97.0825%	154,277,242	156,293,155	98.7102%

PRIMARY VS. REINSURER SHARE OF U.S. MARKET IN 1985 DOLLARS
(000'S OMITTED)

	DOMESTIC PRIMARY (INSUR) WORLDWIDE NET PREM. WRITTEN IN 1985 $			INDUSTRY U.S. DIRECT PREMIUMS WRITTEN IN 1985 $				
	OTHER LIABILITY	COMMERCIAL MULTIPLE PERIL	TOTAL OTHER LIAB & CMP	OTHER LIABILITY	COMMERCIAL MULTIPLE PERIL	TOTAL OTHER LIAB & CMP	DOM. PRIM. PERCENTAGE	REINSURERS PERCENTAGE
1968	4,313,278	2,744,850	7,058,129	4,622,649	3,177,564	7,800,214		
1969	4,709,870	3,081,824	7,791,693	5,051,358	3,543,932	8,595,290		
1970	5,514,696	3,493,449	9,008,145	5,943,852	4,008,905	9,952,757		
1971	6,031,651	4,211,107	10,242,758	6,379,271	4,725,195	11,104,465		
1972	6,265,413	5,115,639	11,381,052	6,567,779	5,657,135	12,224,914		
1973	6,211,833	5,846,033	12,057,865	6,596,951	6,455,660	13,052,611		
1974	6,094,953	5,950,859	12,045,812	6,591,932	6,730,355	13,322,287		
1975	5,692,116	6,028,962	11,721,078	6,372,534	6,917,304	13,289,838		
1976	7,310,853	7,246,691	14,557,544	8,739,970	8,322,199	17,062,170		
1977	9,347,526	8,387,216	17,734,742	11,736,936	9,588,935	21,325,870		
1978	9,878,487	9,243,932	19,122,419	12,787,078	10,695,821	23,482,899		
1979	9,086,679	9,472,770	18,559,449	12,063,635	10,868,114	22,931,749		
1980	7,802,994	8,645,350	16,448,344	10,371,994	10,039,302	20,411,296		
1981	6,601,025	7,749,879	14,350,904	9,078,168	9,138,977	18,217,146		
1982	5,800,434	7,484,820	13,285,254	8,191,956	8,937,542	17,129,497		
1983	5,559,187	7,486,943	13,046,130	8,005,041	8,955,921	16,960,962		
1984	6,182,029	8,165,221	14,347,250	9,158,444	9,840,330	18,998,774		
1985	10,572,927	11,492,552	22,065,479	15,536,966	13,954,330	29,[illegible],296		
SUB-TOTAL	122,975,951	121,848,097	244,824,048	153,796,514	141,557,520	295,354,035	82.8917%	17.1083%
U.S. PERCENTAGE	97.0825%	98.7102%		100.0000%	100.0000%			
U.S. TOTALS	119,388,128	120,276,500	239,664,628	153,796,514	141,557,520	295,354,035	81.1449%	18.8551%

	INFLATION FACTOR
1968	3.09
1969	2.93
1970	2.77
1971	2.66
1972	2.57
1973	2.42
1974	2.18
1975	2.00
1976	1.89
1977	1.78
1978	1.65
1979	1.48
1980	1.31
1981	1.18
1982	1.12
1983	1.08
1984	1.04
1985	1.00

QUALIFIED COMMERCIAL INSURANCE COVERAGES
RELATIVE MARKET SHARES
1968-1985 NET PREMIUMS WRITTEN

(INFLATION ADJUSTED TO 1985 DOLLARS)

	DOMESTIC PRIMARY COMPANIES				DOMESTIC REINSURERS						
Year	CMP	Other Liability	Reinsurance	Total	CMP	Other Liability	Reinsurance	Total	Total Market	Primary Companies' Market Share	Reinsurers' Market Share
1968	$2,733,770	$4,295,866	$35,697	$7,065,333	$138,553	$203,452	$55,136	$397,142	$7,462,475	94.68%	5.32%
1969	3,050,602	4,662,155	37,064	7,749,821	178,573	306,157	62,569	547,299	8,297,120	93.40%	6.60%
1970	3,467,439	5,473,691	44,279	8,985,409	193,188	409,071	74,431	676,690	9,662,099	93.00%	7.00%
1971	4,211,107	6,031,646	65,423	10,308,176	224,711	402,195	126,433	753,339	11,061,515	93.19%	6.81%
1972	5,115,639	6,265,413	85,035	11,466,087	244,497	392,642	159,319	796,458	12,262,545	93.50%	6.50%
1973	5,846,033	6,211,833	132,259	12,190,124	246,714	422,580	263,726	933,021	13,123,145	92.89%	7.11%
1974	5,950,859	6,094,953	145,987	12,191,800	277,024	422,892	287,210	987,125	13,178,925	92.51%	7.49%
1975	6,028,962	5,692,116	118,556	11,839,634	316,864	464,704	249,631	1,031,199	12,870,833	91.99%	8.01%
1976	7,246,691	7,310,853	171,984	14,729,528	403,838	704,061	360,475	1,468,374	16,197,902	90.93%	9.07%
1977	8,387,216	9,347,526	195,462	17,930,203	453,537	1,034,479	413,453	1,901,469	19,831,673	90.41%	9.59%
1978	9,243,932	9,878,487	286,664	19,409,084	363,993	802,654	707,891	1,874,539	21,283,622	91.19%	8.81%
1979	9,472,770	9,086,679	260,317	18,819,765	381,790	670,863	683,293	1,735,946	20,555,711	91.55%	8.45%
1980	8,645,350	7,802,994	220,522	16,668,866	359,603	575,826	651,419	1,586,848	18,255,514	91.31%	8.69%
1981	7,749,879	6,601,025	204,752	14,555,656	343,719	504,910	590,275	1,438,904	15,994,560	91.00%	9.00%
1982	7,484,820	5,800,434	216,724	13,501,978	351,618	524,807	632,408	1,508,833	15,010,811	89.95%	10.05%
1983	7,486,943	5,559,187	191,846	13,237,976	377,579	552,282	645,888	1,575,749	14,813,725	89.36%	10.64%
1984	8,188,774	6,199,862	227,869	14,616,506	454,527	558,014	698,142	1,710,683	16,327,189	89.52%	10.48%
1985	11,492,552	10,572,927	330,187	22,395,666	604,026	971,225	862,635	2,437,886	24,833,553	90.18%	9.82%
Total	$121,803,338	$122,887,647	$2,970,627	$247,661,612	$5,914,353	$9,922,616	$7,524,336	$23,361,305	$271,022,917	91.38%	8.62%
									Arithmetic Average	91.70%	8.30%

Source: A. M. Best's Aggregates and Averages, 1969 to 1986 editions
Inflation adjustments for years 1971 to 1984 per Treasury Department Superfund proposal.
Inflation adjustments for years 1968 to 1971 per CPI.

DOMESTIC REINSURANCE
RELATIVE MARKET SHARE
DOMESTIC PROFESSIONAL REINSURERS and DOMESTIC PRIMARY COMPANIES

(Inflated to 1985 Dollars)

	REINSURANCE NPW BY DOMESTIC REINSURERS		REINSURANCE NPW BY PRIMARY COMPANIES		REINSURANCE NPW BY DOMESTIC COMPANIES
1968	$2,098,873	60.7%	$1,360,267	39.3%	$3,459,139
1969	2,439,166	62.8%	1,444,358	37.2%	3,883,524
1970	2,768,622	62.7%	1,644,127	37.3%	4,412,748
1971	3,234,560	65.9%	1,670,480	34.1%	4,905,040
1972	3,526,040	65.2%	1,881,240	34.8%	5,407,280
1973	3,888,940	66.6%	1,948,100	33.4%	5,837,040
1974	4,022,100	66.5%	2,027,400	33.5%	6,049,500
1975	4,642,000	67.8%	2,204,000	32.2%	6,846,000
1976	5,488,560	67.7%	2,615,760	32.3%	8,104,320
1977	6,463,180	67.9%	3,061,600	32.1%	9,524,780
1978	7,147,800	68.9%	3,225,750	31.1%	10,373,550
1979	6,819,840	72.8%	2,553,000	27.2%	9,372,840
1980	6,341,710	72.9%	2,361,930	27.1%	8,703,640
1981	6,217,420	75.4%	2,029,600	24.6%	8,247,020
1982	6,387,360	76.4%	1,977,920	23.6%	8,365,280
1983	6,788,880	81.7%	1,524,960	18.3%	8,313,840
1984	7,599,298	84.4%	1,409,093	15.6%	9,008,391
1985	9,454,000	84.0%	1,801,000	16.0%	11,255,000
Total	$95,328,349	72.2%	$36,740,584	27.8%	$132,068,933

Source: 1970-1985 Annual Reinsurance Review, published by *National Underwriter*. Amounts reported are based on Annual Statement information from domestic insurers and domestic reinsurers.

Inflation adjustments for years 1971 to 1984 per Treasury Department Superfund proposal.
Inflation adjustments for years 1968 to 1971 per CPI.

DEVELOPMENT OF THE DIRECT AND REINSURANCE BASE

	%			$000,000 Omitted		
	Reinsurer	Direct	Total	Reinsurer	Direct	Total
1. Domestic Professional Reinsurers Net Base -- Since primary insurers net is 81.14% of primary insurers direct (Page 5) and primary insurers net is 91.38% of primary net plus domestic reinsurer net (Page 6) reinsurer % of direct is 7.65%. (.8114 ÷ .9138 = .8879 - .8114 = 7.65)	7.65			$22,595		
2. Offshore reinsurers share of primary insurers direct is 11.21%. 100 - (.8114 + 7.65 = .8879) = 11.21	11.21			33,109		
3. Domestic reinsurers wrote 72.2% of the combined domestic reinsurance market. Therefore, domestic primary insurers market share is 2.95%. (.0765 ÷ 722) = .1060 - .0765 =.0295	2.95			8,713		
4. Net direct is (.8114 - .0295) = .7819		78.19			$230,937	
Subtotal	21.81	78.19	100.00	64,417	230,937	$295,354
5. U.S. risk written by foreign direct writers are estimated to be 5% - 40% of the 5% or 2% is reinsured.	2.00	3.00	5.00	5,907	8,861	14,768
Grand Total	23.81	81.19	105.00	$70,324	$239,798	$310,122

EXHIBIT 2
GENERAL LIABILITY & CMP

Consolidated Industry Totals

	Loss Payment		Allocated LAE Payments		Unallocated LAE Payments		Total Payments		% Ceded:
Accident Year	Dir. & Ass. /	Ceded	Dir. & Ass. /	Ceded	Dir. & Ass. /	Ceded	Dir. & Ass. /	Ceded	Gross
Prior: CY 89-93	11,720.8	6,740.1	5,995.3	2,189.2	278.7	0.0	17,994.8	8,929.3	44.49%
1980 @ 12/31/89	10,454.6	3,884.2	2,220.5	724.3	513.4	0.0	13,168.5	4,608.5	35.00%
1981 @ 12/31/90	11,968.6	4,567.4	2,483.1	760.3	517.1	0.0	14,968.8	5,327.7	35.59%
1982 @ 12/31/91	15,287.6	6,569.9	3,269.2	1,165.2	609.0	0.0	19,165.8	7,735.1	40.36%
1983 @ 12/31/92	18,774.2	8,664.1	3,984.7	1,543.1	675.9	0.0	23,434.8	10,207.2	43.56%
1984 @ 12/31/93	22,192.0	10,426.5	5,157.3	2,108.4	757.7	0.0	28,107.0	12,534.9	44.60%
1985 @ 12/31/93	23,308.9	9,407.0	5,470.2	1,957.4	854.3	0.0	28,633.4	11,364.4	39.69%

	Loss Payment		Allocated LAE Payments		Unallocated LAE Payments		Total Payments		% Ceded
Cal Year Period	Dir. & Ass. /	Ceded	Dir. & Ass. /	Ceded	Dir. & Ass. /	Ceded	Dir. & Ass. /	Ceded	Gross
85 &Prior: CY 90	7,397.6	4,435.0	2,846.2	1,085.7	(9.7)	0.0	10,234.1	5,520.7	53.94%
85 &Prior: CY 91	5,259.0	3,240.1	2,684.6	1,202.1	89.3	0.0	8,032.9	4,442.2	55.30%
85 &Prior: CY 92	5,143.1	2,735.0	2,074.1	893.3	103.8	0.0	7,321.0	3,628.3	49.56%
85 &Prior: CY 93	4,626 0	2,956.2	1,946.2	752.2	132.5	0.0	6,704.7	3,708.4	55.31%
Total: CY 90-93	22,425.7	13,366.3	9,551.1	3,933.3	315.9	**0.0**	32,292.7	17,299.6	**53.57%**

Source: Bests Aggregate & Averages

EXHIBIT 3
GENERAL LIABILITY & CMP

Consolidated Industry Totals

	Losses Unpaid				ALAE Unpaid								
	Case Basis		Bulk & IBNR		Case Basis		Bulk & IBNR		Unallocated		Tot. Loss & LAE Reserve		
	Dir. & Ass	Ceded	Dir. & Ass	Ceded	Dir. & Ass	Ceded	Dir. & Ass	Ceded	Dir. & Ass	Ceded	Dir. & Ass	Ceded	% Ceded
AETNA	242.8	49.0	339.4	44.3	132.1	47.8	287.5	15.5	22.6	0.0	1,024.4	155.6	15.29%
Allstate	621.8	224.8	977.7	375.3	107.1	38.3	220.8	141.6	12.7	0.0	1,940.1	780.0	40.20%
AmerFinancial	170.5	68.7	94.1	44.0	29.8	13.8	10.0	3.3	7.1	0.0	311.5	729.8	41.67%
AIG	1,220.5	1,005.0	552.5	483.3	23.3	18.3	179.2	107.2	0.1	0.0	1,975.6	1,613.8	81.69%
Chubb	268.9	41.7	136.6	12.4	112.7	13.5	44.9	7.7	3.6	0.0	566.7	75.3	13.29%
CIGNA	787.1	414.9	308.7	193.6	0.0	0.0	146.7	104.1	0.1	0.0	1,242.6	712.6	57.35%
CNA	530.6	166.6	2005.9	208.8	0.0	0.0	54.5	12.6	2.2	0.0	2,593.2	388.0	14.96%
Comm Union	63.8	37.1	52.5	7.0	44.4	10.4	20.3	0.0	3.5	0.0	184.5	54.5	29.54%
Continental	398.0	177.0	36.3	12.4	0.0	0.0	21.6	8.7	2.0	0.0	457.9	198.1	43.26%
Crum & Forster	1,499.1	1,432.0	1,012.4	601.3	177.3	149.8	95.2	62.4	31.1	0.0	2,815.1	2,245.5	79.77%
Farmers	13.0	4.0	48.6	11.9	0.0	0.0	13.1	(14.6)	1.6	0.0	76.3	23.3	30.54%
Fireman's Fund	251.9	115.9	247.0	87.2	4.8	2.0	155.2	49.4	7.0	0.0	665.9	254.5	38.22%
Home Ins Group	371.8	295.2	200.7	168.9	0.0	0.0	94.7	60.6	9.1	0.0	676.3	524.7	77.58%
ITT Hartford	361.2	136.5	668.3	240.6	79.0	16.0	302.5	39.8	13.1	0.0	1,424.1	432.9	30.40%
Kemper	88.6	34.8	0.0	0.0	115.5	10.3	0.0	0.0	22.3	0.0	226.4	45.1	19.92%
Liberty Mutual	409.2	28.4	227.6	3.9	0.4	0.0	463.1	24.7	38.4	0.0	1,138.7	57.0	5.01%
Lincoln National	48.5	10.5	17.2	0.0	12.5	2.2	4.1	0.0	3.7	0.0	85.3	12.7	14.89%
Nationwide	254.0	95.9	85.0	39.5	4.5	3.4	92.4	29.0	2.3	0.0	438.1	167.8	38.29%
Reliance	67.3	28.1	22.9	10.4	0.0	0.0	54.5	18.4	1.8	0.0	146.5	56.9	38.84%
Royal	210.7	52.5	122.2	45.5	100.1	21.8	38.7	14.1	4.3	0.0	476.0	133.9	28.13%
St. Paul	198.7	77.4	24.9	4.2	38.0	9.5	9.0	0.3	3.9	0.0	274.5	91.4	33.30%
State Farm	13.6	2.5	4.4	0.0	0.1	0.0	8.4	0.0	0.8	0.0	27.3	2.5	9.16%
Travlers	185.9	72.1	440.7	136.9	96.8	33.0	308.2	73.8	26.7	0.0	1,058.3	315.8	29.84%
USF&G	120.1	19.2	97.6	2.2	0.0	0.0	63.8	(0.4)	13.8	0.0	295.3	21.0	7.11%
Zurich	72.4	38.1	58.4	1.8	36.2	0.0	26.0	0.2	6.6	0.0	199.6	40.1	20.09%
Total of Above	8,470.0	4,627.9	1,781.6	2,757.4	1,114.6	390.1	2,714.4	758.4	239.7	0.0	20,320.3	8,533.8	42.00%
Industry	16,051.3	10,277.0	14,037.5	6,716.7	1,915.9	939.8	3,766.5	1,466.2	323.9	0.0	36,095.1	19,399.7	53.75%

11786 net prem
166795 70.6%
reserve accident years
56% of gross reserves

Source: Best Aggregates & Averages
& Best Reproductions of Annual Statements

PREPARED STATEMENT OF LESLIE B. SAMUELS

Mr. Chairman and Members of the Committee: I am pleased to discuss today the Administration's proposals for funding the reauthorization and amendment of the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA) contained in the Superfund Reform Act of 1994 (S. 1834). CERCLA created the Superfund program, which is the Federal government's primary program for addressing dangerous environmental and health conditions created by the release of hazardous substances into the environment.

Before describing the specific financing elements connected with the Administration's proposal, I would like to briefly summarize the Superfund reform legislation and the state of affairs under current law.

CURRENT LAW

Superfund Trust Fund

CERCLA provides the Federal government with the authority to respond to and clean up releases of hazardous substances into the environment. Under CERCLA, the Environmental Protection Agency (EPA) has two tools for cleaning up hazardous waste sites. First, EPA can take legal action to force responsible parties to clean up contaminated sites or to reimburse the Federal government for the cost of the cleanup. Second, EPA can use funds in the Hazardous Substance Superfund trust fund to finance the cleanup of hazardous waste sites where a responsible party cannot be found or is not financially viable (orphaned sites). The trust fund can also be tapped to expedite the cleanup of other sites where costs will ultimately be recovered from potentially responsible parties (PRPs).

The Superfund trust fund is currently financed primarily by excise taxes on domestic crude oil, imported petroleum products, certain chemicals and imported derivative products, a corporate environmental tax, and annual appropriations from general revenues. More specifically, the trust fund is financed by the following taxes: (1) an excise tax on crude oil and imported petroleum products equal to 9.7 cents per barrel for domestic crude oil received at a United States refinery or exported, on imported crude oil, and imported petroleum products entered into the United States for consumption, use, or warehousing; (2) excise taxes imposed on listed chemicals sold domestically or used by the manufacturer, producer, or importer of the listed chemicals at rates ranging from $0.22 to $4.87 per ton; (3) excise taxes on certain imported derivative products generally at rates applicable to taxable chemicals used as materials in the manufacture of the imported substances; and (4) the corporate environmental tax equal to 0.12 percent of modified alternative minimum taxable income in excess of $2 million.

These taxes are scheduled to expire on December 31, 1995. However, the taxes may terminate earlier if amounts in the Superfund trust fund reach certain levels. The Superfund taxes may expire before January 1, 1996 if (1) on December 31, 1994, the unobligated balance in the Superfund exceeds $3.5 billion and will exceed $3.5 billion at the end of the following year if no Superfund taxes were imposed during the year, or (2) if the amount of cumulative Superfund taxes collected exceeds $11.97 billion.

The Superfund taxes provide an adequate and stable source of funds for the trust fund. In enacting CERCLA, Congress decided that the cleanup costs incurred by the Federal government where a private party could not be identified or was not financially viable should be paid by current producers and users of hazardous substances. By taxing the materials used to make hazardous products and waste, these costs would be borne by persons producing or using hazardous materials. Accordingly, Congress enacted the excise taxes on petroleum and chemicals.

Under the Superfund Amendments and Reauthorization Act of 1986, Congress decided to expand the Superfund financing sources to include the corporate environmental tax. The addition of this broad-based funding source reflected the view that the production and use of hazardous substances and the benefits from cleanup were widely dispersed.

Litigation

CERCLA imposes liability for cleanup costs on current owners and operators of disposal sites, owners and operators at the time of a release, and generators and transporters of hazardous substances. Responsible parties are subject to strict, joint, and several liability standards with respect to costs associated with the removal and cleanup of hazardous substances. This liability system currently generates a significant amount of litigation for recoveries between EPA and PRPs (enforcement litigation), between initially identified PRPs and other PRPs (contribution litigation), and

PRPs and their insurers (insurance litigation). As a result, litigation costs have been and continue to be significant.

Insurers that wrote commercial liability and comprehensive general liability coverage prior to January 1, 1986 sometimes have to pay claims related to a policyholder's liability for cleanup costs, either because the insurance contracts specifically included coverage for environmental liability losses or the judicial system determines that the insurer is liable under the terms of the insurance contract for cleanup costs incurred by the policyholder. The costs incurred by PRPs and insurers in insurance litigation are significant. That money would be better spent cleaning up hazardous waste sites.

OVERVIEW OF PROPOSED LEGISLATION

Superfund Trust Fund

S. 1834 contains reform initiatives that fulfill the Administration's commitment to protecting human health and the environment and to making Superfund cleanups faster, fairer, and more efficient. It is our belief that the Administration's proposed financing provisions provide an adequate and stable financial base for the Superfund.

S. 1834 would reauthorize the Superfund program at $9.6 billion for the five year period beginning October 1, 1994 and ending September 30, 1999. The legislation would extend the existing Superfund taxes for five years and would authorize the present level of appropriations from general revenues for the Superfund ($250 million per year for FY 1995 through FY 1999).

The present excise taxes would be extended until December 31, 2000. The corporate environmental tax would be extended through taxable years beginning before January 1, 2001. No changes are proposed in the present tax rates or taxable substances. However, under the Administration's proposal the ceiling on total Superfund taxes that can be collected without causing the taxes to cease would increase from $11.97 billion to $22 billion. This increase in the ceiling should permit the reauthorized taxes to be collected; otherwise the taxes could terminate prematurely when the lower ceiling is hit.

Litigation

Title VIII of S. 1834 is designed to reduce the costly litigation between PRPs and their insurers. A new Environmental Insurance Resolution Fund (EIRF) would be established with the objective of facilitating settlement of the vast majority of litigation involving insurance claims related to Superfund or environmental liability.

Under present law, protracted disputes between insurance companies and their policyholders regarding the applicability of coverage to liability under CERCLA are a major source of litigation related to Superfund. The legislation will reduce this litigation and allow monies that would otherwise be spent in adversarial proceedings to be used for cleanup.

The EIRF would make a single, comprehensive offer to each eligible responsible party to resolve all pending and future claims of the policyholder against its insurers arising under the Superfund law for eligible costs of the policyholder. A policyholder that accepted the EIRF's offer would be reimbursed at a fixed percentage of its eligible costs and would be required to waive all current and future CERCLA-related claims against its insurers. If a policyholder rejects the EIRF's offer, the EIRF would reimburse insurers for litigation costs and judgment amounts associated with any litigation brought by that policyholder, up to the amount of the offer.

The Administration's original funding proposal for the EIRF was designed to raise $3.1 billion over five years, consistent with the terms of the Administration's original reform proposal. When the Senate Committee on Environment and Public Works favorably reported the bill, the term of the reform proposal was extended beyond five years to an anticipated term of ten years. As a result of the extension of the EIRF's term, and in conjunction with the consideration of the bill by the House Committee on Ways and Means, we revised our proposal to raise $810 million per year over the term of the EIRF.

Now, I would like to describe the Administration's proposed financing mechanism for the EIRF and the rationale behind it. The proposal that I will describe is the proposal that was favorably reported by the House Committee on Ways and Means with some modifications. The modifications reflect extensive discussions that have taken place over the last few weeks. First, I will describe the modified proposal and I will conclude by summarizing the changes from the bill reported by the Committee on Ways and Means.

OVERVIEW OF ENVIRONMENTAL INSURANCE RESOLUTION REFORM FUNDING

To determine how to finance equitably the EIRF, we met with many insurance industry representatives to gain a better understanding of the Superfund problems and issues arising from various proposals. In the context of these extensive and ongoing discussions, we developed three principles that provided guidance for financing proposals for the EIRF. The fundamental principles are: (1) insurers that potentially benefit from the environmental insurance resolution reform—those that have potential Superfund liabilities through commercial insurance coverage written in the past-should provide a significant portion of the EIRF's funding; (2) the commercial insurance industry as a whole, its policyholders, and society also will benefit from the reform and should pay some portion of the EIRF's funding; and (3) all commercial insurers and reinsurers, whether domestic or foreign, that insure risks in the United States benefit from the reform and should participate in its funding.

Given these three principles, we reached what we believe is a reasonable approach for financing the EIRF whose framework is supported by a significant segment of the industry. Under the proposal, the financing of the Fund would be split nearly equally, on a present value basis, between retrospective and prospective taxes.

During the first four years, approximately 69 percent of the financing for the EIRF would be obtained from separate retrospective taxes on those insurers and reinsurers that wrote certain commercial liability coverage in the past, with 46 percent of the total financing coming from a tax on direct insurers and 23 percent of such financing coming from a tax on reinsurers. Approximately 31 percent of the financing for the EIRF would be raised by a prospective tax on direct premiums written by insurers for insurance coverage of U.S. risks in commercial lines of business after the date of enactment.

During years five through ten, 66 percent of the funding would be raised by the prospective tax on direct premiums written for insurance coverage of U.S. risks in commercial lines of business. The remaining 34 percent would be obtained from a retrospective tax on reinsurance premiums (23 percent of total revenues), and an assessment on insurers that wrote coverage that gave rise to actual Superfund claims for which the EIRF makes awards (11 percent of total revenues).

The annual financing of the Fund would be as follows:

Years	Retrospective Tax on Direct Insurance	Retrospective Tax on Reinsurance	Prospective Tax	Assessments on Insurers
1–4	$374 million	$188 million	$248 million	$0
5–10	$0	$188 million	$537 million	$85 million

To provide the insurance industry with assurances that the taxes to be collected would not exceed their revenue targets, the amount of taxes collected under the prospective tax, the retrospective tax on direct insurers, and the retrospective tax on reinsurance premiums would be subject to separate multi-year caps that would limit the actual collections to the targeted amounts. Each tax would trigger off when the appropriate revenue is raised within multi-year timeframes. Those timeframes have not yet been determined. However, we would suggest that the Committee consider two multi-year periods—years one through four and years five through ten. If the amount collected for a particular tax reached its revenue cap, that tax would not be collected for the remainder of the period for which the cap applies.

In addition, separate multi-year caps would apply to the retrospective tax collected on domestic and foreign reinsurance premiums. These separate caps would be proportional to the reasonably estimated share of the domestic and foreign markets and established to reduce the risk of a revenue shortfall for the Fund. In addition, the retrospective taxes on reinsurance premiums would also be subject to an overall multi-year cap of 23 percent of the EIRF's total revenues.

The Fund could have continuing obligations beyond its anticipated 10-year term. Treasury would conduct a study in the ninth year of the Fund to make recommendations with respect to the insurance industry's financing of the Fund after the tenth year. Absent Congressional action, the funding provided in the proposal would continue until all ongoing obligations of the Fund are satisfied.

Under this proposal and consistent with our first principle that those that potentially benefit the most from reform should pay for a significant share of the reform, the taxes and assessments that are retrospectively based would be paid by those insurers and reinsurers that could potentially benefit most from reform. The assessments would be imposed on insurers that wrote coverage that gave rise to actual

Superfund claims for which the EIRF makes awards. The excise taxes that use a retrospective computation basis would be imposed on net premiums written by domestic and foreign insurers and reinsurers for contracts insuring certain U.S. commercial liability risks during the period from 1968 through 1985.

We believe that the base period of 1968 through 1985 for determining commercial net written premiums is a reasonable approach to develop the retrospective tax base. Any insurer or reinsurer that wrote coverage for losses arising from comprehensive general liability or commercial multiperil liability risks situated in the United States prior to 1986 has potential exposure to environmental liability claims as policyholders discover that they are PRPs. This exposure generally ceased in 1986 because insurers began including in their insurance contracts a specific exclusion for coverage of claims related to environmental liability. Although the exposure ends in 1986 but extends back in time, we thought it would be inappropriate to require insurers to search back in time for records that may be difficult to locate or may not be reliable. Publicly available data prior to 1968 are less reliable and so we only extended the start of the base period for determining this retrospective tax back to 1968.

Consistent with the second principle that the entire insurance industry, policyholders, and society benefit from reform and should participate in the EIRF's financing, the prospective tax would be borne both by insurers that benefit from reform and more broadly by others. The prospective tax would be imposed on future direct premiums from insurance of U.S. risks written in commercial lines of business by domestic and foreign insurers.

A tax imposed on future direct premiums written by insurers has merit in funding a portion of the EIRF. The health of the industry would be improved by environmental insurance resolution reform and the potential for state guaranty fund involvement would be reduced. If insurance companies liable for environmental claims become insolvent, State guaranty funds can assess solvent insurers to pay outstanding policyholder claims of insolvent insurers. Thus, all insurers (and their policyholders) may ultimately benefit from the proposed reform, regardless of whether an insurer wrote coverage that directly generates environmental exposure. Also, given the possibility that a part of the tax on future premiums might be passed through to policyholders, the tax would be borne more generally by consumers of the insurance coverage. For these reasons, a portion of the financing should be provided by insurers writing commercial coverage today.

The prospective tax would be imposed on a broader base of premiums than the retrospective tax primarily to preserve the stability and predictability of the tax base. A prospective tax relies on premiums being reported in the lines of business subject to the tax. If the tax is imposed on too few lines of business, there could be potential for erosion of the premium base as insurance is repackaged and sold in a different manner. Also, if the tax is imposed on too few lines, the premium base is small and forces the tax rate to be high. Due to the competitiveness and price sensitivity in the commercial insurance market, a high tax rate on too few lines of business could cause an erosion of the tax base as policyholders may choose to self insure.

Consistent with the third principle, that all insurers and reinsurers should participate in the EIRF funding, the Administration's proposal requires foreign insurers and reinsurers to contribute their fair share through taxes and assessments. Foreign insurers and reinsurers that are currently subject to net-basis U.S. income taxation would pay the retrospective taxes on the same basis as would domestic insurers and reinsurers. Alien insurers and reinsurers (i.e., foreign insurers that are not subject to net-basis U.S. income taxation) would be required to participate in the EIRF funding in a different manner. To ensure that alien insurers and reinsurers contribute to the EIRF, their U.S. insurance contracts would be subject to a prospective tax on coverage limits, collected by a U.S. withholding agent, in lieu of the retrospective tax. Alternatively, an alien insurer or reinsurer could elect to be subject to the retrospective tax and assessments, in lieu of the tax on coverage limits, by making an election, if certain conditions are met, or entering into a closing agreement with the Internal Revenue Service. In addition, insurers and reinsurers would be required to identify to the Internal Revenue Service at the time of their first retrospective tax filing their foreign reinsurers and, with good faith effort, the amounts of qualified commercial insurance ceded to those foreign reinsurers during the period from 1968 to 1985.

Both foreign and alien insurers would pay the prospective tax imposed on certain direct insurance premiums on the same basis as domestic insurers. In the case of alien insurers, the tax would be collected by a U.S. withholding agent.

FUNDING SPECIFICS OF ENVIRONMENTAL INSURANCE RESOLUTION REFORM

Retrospective Taxes

The retrospective taxes are designed to raise $3.376 billion over ten years ($2.248 billion for years one through four and $1.128 for years five through ten). These taxes would be determined by multiplying the applicable tax rate by the adjusted base-period commercial premiums written for contracts or agreements providing insurance or reinsurance with respect to qualified commercial coverage of risks within the United States (including Puerto Rico, and any U.S. possessions and territories) during the period beginning January 1, 1968, and ending on December 31, 1985. For years one through four, an applicable tax rate would be determined that would raise $374 million annually from net direct insurance premiums and $188 million from net reinsurance premiums. After year four, the applicable reinsurance premium tax rate would remain the same and the applicable direct tax rate would be zero.

Separate multi-year caps would limit the amount of tax collected from premiums for net direct insurance premiums to $374 million per year for four years and from net reinsurance premiums to $188 million per year for ten years. We would suggest that the caps be imposed in four and six-year intervals. In years one through four, the cap at which the taxes trigger off would be four times the annual target revenue. In years five through ten, the cap at which the taxes trigger off would be six times the annual target revenues. In addition, separate multi-year caps would apply to the retrospective tax collected on foreign and domestic reinsurance premiums. These caps would be proportional based upon the foreign and domestic reinsurers' reasonably estimated market shares and established to reduce the risk of an overall revenue shortfall to the Fund. They would also be subject to the overall multi-year cap of $188 million per year on the retrospective tax on net reinsurance premiums.

1. *Adjusted base-period commercial premiums.* In determining the total adjusted base-period commercial premiums written for 1968 through 1985 to which the funding rates are applied, the net premiums written for each year during the period for qualified commercial insurance contracts and reinsurance of qualified commercial insurance coverage would be adjusted by an inflation factor based on the consumer price index. This inflation adjustment would restate all premiums written to 1985 dollars so that they are taxed on a comparable basis.

2. *Exclusions.* In determining adjusted base-period commercial premiums, $50 million would be excludable from inflation-adjusted base-period commercial direct premiums. One $50 million exclusion would be available to certain "related" parties. This exclusion is intended to provide relief to small insurers and mitigate any mistargeting of the premiums proxy. No exclusion is provided for reinsurance premiums. However, the Secretary of the Treasury would have the authority to specify an exception that would exclude base-period reinsurance premiums of a de minimis amount.

3. *Net premiums written for qualified commercial insurance contracts.* Net premiums written for qualified commercial insurance contracts means net premiums written for contracts providing insurance of qualified commercial coverage of U.S. situs risks generally computed on the basis of the annual statements approved by the National Association of Insurance Commissioners (NAIC).

Qualified commercial coverage means insurance coverage that was, or should have been, characterized in the NAIC annual statement as "commercial multiple peril" or other liability" lines of business. However, contracts included in the "other liability" line of business that insured only specific coverages unrelated to general commercial liability, and thus would not generate exposure to environmental insurance claims, would be excluded. For example, medical malpractice insurance would be an excludable coverage. However, commercial property damage insurance, for example, could not be excluded from the commercial multiple peril line of business.

For insurers and reinsurers not filing NAIC annual statements, net written premiums should be computed on a basis comparable to that required by the NAIC using reasonable methods (as approved or provided by the Secretary) to approximate comparability where necessary due to inadequate books and records.

4. *Net premiums written for allocated reinsurance of qualified commercial coverage.* Premiums related to allocated reinsurance (i.e., generally first dollar pro rata reinsurance) are identified by line of business. Accordingly, net premiums written for allocated reinsurance of qualified commercial coverage means net premiums written for reinsurance which were reported (or, in the case of a company not filing an annual statement, would have been required to be so reported) on the annual statement approved by the NAIC by the line of business related to the underlying policies covered by such reinsurance, rather than on the reinsurance line of business of the annual statement.

5. *Net premiums written for unallocated reinsurance of qualified commercial coverage.* For certain reinsurance coverage (e.g., reinsurance in excess of a retention by the ceding company), the reinsurer may not have separately reported net premiums written by line of business on the annual statement. The reinsurer often cannot identify or directly trace the type of insurance coverage to which the premiums relate because several types of insurance coverage could be combined in the reinsurance agreement. Thus, the net premiums written for this unallocated reinsurance would be determined using a formula, or proxy approach, based on the insurance industry's ceded premiums for qualified commercial coverage from January 1, 1968, through December 31, 1985.

To derive the net premiums written related to unallocated reinsurance of qualified commercial coverage, a reinsurance ratio of 21 percent would be multiplied by the net premiums written, as reported on the NAIC annual statement (or equivalent computational basis if an NAIC annual statement was not prepared) for the reinsurance line of business.

6. *Foreign insurers and reinsurers.* Foreign persons (including foreign companies, partnerships, trusts, and estates and nonresident alien individuals) that insure or reinsure U.S. risks would be subject to the retrospective taxes if they are currently engaged in any trade or business within the United States and their taxable income that is effectively connected with that trade or business is subject to net-basis U.S. income taxation and is not exempt by treaty from such taxation. The retrospective taxes would be computed in the same manner as for U.S. insurers and reinsurers.

All other foreign insurers and reinsurers ("alien insurers and reinsurers") would be subject to a prospective "limits" tax in lieu of the retrospective taxes and assessments, unless they elect to be subject to the retrospective taxes and assessments. This prospective limits tax would be imposed at a rate of 0.50 percent of the maximum limit of liability on each policy of casualty insurance insuring or reinsuring U.S. risks. The tax would be imposed on all lines of casualty business, broadly defined, to prevent alien insurers and reinsurers from avoiding the tax simply by ceasing to write qualified commercial insurance coverage in the United States. The tax would be withheld and remitted to the Internal Revenue Service by the U.S. premium payor or other U.S. withholding agent.

Alternatively, alien insurers and reinsurers could elect to be subject to the retrospective taxes and assessments. If such an election were made, the retrospective taxes and assessments would apply in the same manner as they apply to U.S. insurers and reinsurers (and to other foreign insurers and reinsurers). Electing aliens would be required to enter into a closing agreement with the Internal Revenue Service to ensure collection of the retrospective taxes and assessments. However, foreign persons would preliminarily elect, pending execution of a closing agreement, to be subject to the retrospective taxes in lieu of the limits tax. Under such an agreement, in place of requiring immediate payment and withholding of the limits tax, the insurer or reinsurer would be required to post adequate security in a designated form with the Treasury for payment of the taxes. If a closing agreement was not executed within a reasonable period of time, the Treasury would be entitled to collect the full amount of limits tax, including the retention of any posted security.

Electing alien insurers that do not have adjusted base-period commercial premiums would not be required to enter into a closing agreement with respect to the retrospective taxes and assessments if certain expedited procedures are followed.

7. *Corporate reorganizations.* Special rules designed to prevent erosion of the retrospective tax base are also provided to ensure that the tax follows the commercial insurance business of a company in any corporate reorganization involving an acquisition or disposition of all, or a part, of a company's commercial insurance business. Rules also address movement of the tax in assumption reinsurance transactions and the commutation of reinsurance transactions.

Prospective Tax

The prospective tax is designed to raise $4214 billion over ten years ($0.992 billion for years one through four and $3.222 billion for years six through ten). A tax on an insurer's direct premiums written after the date of enactment, in excess of an exemption amount, for insurance in commercial lines of business would finance the Fund. The prospective tax rate would be determined that would raise $248 million annually for the first four years, and $537 million annually for years five through ten. The exemption amount is generally $5 million per year and must be shared by certain "related" parties. It is designed to lessen the burden on small insurers and takes many small insurers completely out of the tax.

The prospective tax would be subject to multi-year caps that would limit the amounts collected to the targeted revenue amounts. We would suggest a cap for the

first four years of $992 million ($248 million times four) and $3.222 billion ($537 million times 6) for the next six years.

The tax would apply in the same manner with respect to insurance contracts written by foreign insurers of U.S. risks. It would be collected through withholding in the case of alien insurers.

Direct premiums written for commercial insurance contracts means gross premiums written and other consideration for contracts providing insurance of coverage of risks wholly or partly within the U.S. (including Puerto Rico, and any U.S. possessions and territories) for which the premiums are, or should be, reported in a commercial line of business. Gross premiums written would be computed on the basis of the annual statement approved by the NAIC or on an equivalent basis.

Insurance in commercial fines of business would include insurance that is, or would be, categorized in the NAIC annual statement exhibit of premiums and losses as fire, allied lines, farmowners multiple peril, commercial multiple peril, ocean marine, inland marine, products liability, other liability, commercial auto no-fault, other commercial auto liability, commercial auto physical damage, aircraft, surety, glass, burglary and theft, and boiler and machinery. Other lines of business would be excluded: multiple peril crop, homeowners multiple peril, financial guaranty, mortgage guaranty, medical malpractice, earthquake, accident and health, workers' compensation, private passenger auto no-fault, other private passenger auto liability, private passenger auto physical damage, fidelity, and credit. Premiums written for an insurance policy that provides directors and officers liability insurance, professional liability insurance, and insurance for fire, other perils, or extended coverage on residential or farm owner-occupied housing units would not be subject to the prospective tax, even though the premiums for such coverage would be reported in a covered line of business. In addition, the following personal insurance policies, the premiums from which are included in covered lines of business, would be excluded: personal liability umbrella, personal articles, personal owner-used boats, and property damage and liability coverage for owner-occupied condominium associations.

The Secretary of the Treasury would have the authority to extend the prospective tax to lines of coverage other than those specifically identified only as necessary to respond to changes in the construction of the annual statement lines originally covered. The Secretary's authority would not extend to the inclusion of any reinsurance coverage.

Assessments on Direct Insurers

The assessments on direct insurers are designed to raise $85 million annually beginning in the fifth year. The assessments would be based on awards paid by the EIRF with respect to policies issued during certain periods by the insurer.

The amount of the annual assessment is determined by multiplying the insurer's share of the aggregate coverage limits of all assessable policies by $85 million. The insurer's applicable share is determined by dividing the coverage limits on all the insurer's assessable policies by the total coverage limits for such policies for all direct insurers.

An assessable policy must be a valid insurance contract that was presented to the EIRF for an award and with respect to which the EIRF made a resolution payment to an eligible party during any of the four years preceding the year in which the assessment is imposed. The coverage limit on a policy is generally the aggregate limit of coverage under the policy, determined without regard to deductibles or any self-insured retention. Insurers would be permitted to reduce the coverage limit of an assessable policy by 80 percent of the amount of the coverage that is reinsured.

EFFECTIVE DATES

The prospective and retrospective taxes and assessments generally would be effective on January 1, 1995, unless otherwise provided in the proposal. The prospective tax would apply to policies for which direct premiums are written on or after January 1, 1995. The limits tax on foreign persons would be imposed on policies for which premiums are written after the date the Fund becomes operational as described below. The assessments on insurers would become payable beginning in 1999, the fifth year of the Fund.

The Fund could have continuing obligations beyond its anticipated ten-year term. A Treasury study would be conducted in the ninth year of the Fund to make recommendations with respect to the insurance industry's financing of the Fund after the tenth year. Absent Congressional action, the funding provided for in the proposal would continue until all ongoing obligations of the Fund are satisfied. No inference is intended by the proposed allocation in any year, or combination of years, between retrospective and prospective taxes and assessments with regard to the

structure of any tax or assessment that the Congress may find necessary to enact in the future.

The authorizing legislation (S. 1834) accompanying this proposal provides that the Fund would not become operative if more than 20 percent of all eligible potentially responsible persons reject resolution offers from the Fund. If between 15 and 20 percent of such persons decline to participate in the Fund, the Fund could decide whether to continue or terminate the Fund. This determination would be required to be made within 225 days from the date of the bill's enactment.

To finance the operations of the Fund during this 225-day contingency period, start-up filing fees of approximately $1 million would be imposed on insurers by the Fund. These fees would not be creditable against any retrospective or prospective tax or assessment imposed under the Internal Revenue Code.

The retrospective and prospective taxes would accrue during the 225-day contingency period but would not be payable during such period. The taxes would not be collected until it is determined that the Fund has adequate participation. On the 14th day of the month beginning after the end of the contingency period, if adequate participation is achieved, the retrospective and prospective taxes that accrued during the contingency period would be due and payable.

Once the Fund becomes operational, the retrospective, prospective, and limits taxes would be payable on a monthly basis. For purposes of the prospective tax, estimated amounts could be paid for months in which premium data is not readily available. However, accurate calculation and payment of the prospective tax would be required on a quarterly basis.

Although generally the prospective tax would apply to premiums written after date of enactment but would not become payable by insurers until the contingency period ends, the effective date for imposition of the prospective tax for insurers not otherwise subject to U.S. income tax would be delayed until the contingency period ends. These insurers would be subject to the prospective tax for premiums written until the date that is the number of days in the contingency period beyond December 31, 1994, or the date that all of the Fund's obligations are satisfied, if later.

If the Fund does not become operational, any remaining amounts in the Fund would revert to the general revenues of the Treasury.

Tax Exemption

The EIRF would be exempt from Federal income tax under Section 501.

Summary

In summary, the proposal submitted to the Committee today satisfies the three principles discussed earlier. It would require insurers that could potentially benefit the most from the environmental insurance resolution to provide a significant share of the funding. Approximately 50 percent of the financing would be raised from retrospective taxes and from assessments on direct insurers that wrote coverage for which the EIRF makes resolutions. The retrospective taxes are paid in the future. They replace an existing, but uncertain liability arising from commercial insurance coverage written in the past—the policies with potential environmental liability exposure. The retrospective taxes will likely reduce profits of insurers subject to the taxes and be borne largely by their current shareholders, who also would bear the continued cost of environmental liability claims and litigation costs associated with these claims. The proposal provides some relief by allowing an exclusion of $50 million from the retrospective base of direct premiums and an exclusion for certain types of coverage in the "other liability" line of business that have no potential exposure to environmental liability claims.

The other 50 percent of the financing is more broadly based and is raised from a prospective tax on premiums written for insurance categorized in commercial lines of business. The broad base of commercial insurance business subject to this tax reflects the industrywide nature of the environmental problem. To ensure a predictable and stable revenue source for the EIRF, the premium base broadly encompasses most lines of business that are commercial in nature. An annual $5 million exemption of premiums mitigates for small insurers some of the effect of the tax.

We understand that as a result of market forces insurers are not expected to be able to pass the prospective tax through to their reinsurers. Because reinsurers would not pay the prospective tax, but would potentially benefit from reform, they would contribute to the financing through retrospective taxes. The direct writers would contribute to the financing through a combination of retrospective taxes and assessments, as well as through prospective taxes.

The proposal would also assure that foreign insurers and reinsurers that potentially benefit from the proposed reform participate in its funding. While a foreign insurer could avoid participation in the financing of the EIRF if that insurer stopped

writing all types of property/casualty insurance coverage in the United States, we believe that this is highly unlikely given the importance of the U.S. market.

The proposal I have described contains certain changes from the bill reported by the Committee on Ways and Means. The following briefly highlights those changes: (1 Reinsurers would participate in the financing through a retrospective tax rather than a combination of retrospective taxes and assessments. Reinsurers originally requested to be subject to assessments but later reconsidered because the assessments created considerable complexity; (2) The $50 million exclusion amount from the retrospective tax base would be allocated entirely to direct insurance premiums, rather than allocated proportionately between direct and reinsurance premiums. Thus, the $50 million exemption would not be available for reinsurance. This change would broaden the tax base and permit lower tax rates on reinsurance premiums under the retrospective tax; (3) The Secretary of the Treasury's authority to extend the prospective tax to lines of coverage other than those originally identified as covered lines would be clarified to provide that such authority is intended to allow the Secretary to respond to changes in the construction of the lines, and does not extend to reinsurance; (4) The target revenue amounts to be raised from the prospective tax, the retrospective tax on direct premiums, and the retrospective tax on reinsurance premiums, would be adjusted slightly (the target for the retrospective tax on reinsurance would be reduced by $12 million per year and this $12 million would be allocated to the other taxes and assessments) and separate multi-year caps would be imposed to limit actual collections to the target revenue amounts; (5) Separate multi-year caps would be established for the taxes paid by domestic and foreign reinsurance premiums based on their reasonably estimated, proportional market shares and to reduce the risk of a revenue shortfall for the EIRF. These multi-year caps ensure that domestic and foreign reinsurers do not overcontribute to the Fund; (6) Insurers and reinsurers would be required to identify using good faith efforts their foreign reinsurers and amounts of insurance ceded to foreign reinsurers from 1968 through 1985. This change is intended to improve compliance with the retrospective tax; (7) The prospective tax base would be modified to exclude certain policies of personal insurance and financial guaranty and fidelity insurance; (8) Absent Congressional action, the funding provided for in the proposal would continue until all ongoing obligations of the Fund are satisfied; and (9) Periodic reports would provide data on taxes received from each of the proposal's sources of tax and from domestic and foreign sources.

CONCLUSION

There has been considerable controversy within the insurance industry about how the funding for the EIRF should be structured. Some insurers have argued that the funding mechanism should be entirely retrospective, i.e., based on commercial insurance business written in the past. Others have argued that the funding should be entirely prospective, i.e., based on commercial insurance business written in the future. We believe that our proposal represents a reasonable approach. Insurers and reinsurers that write approximately 60 percent of the Fund's taxable premiums support the framework I have described to finance the Fund. Understandably, they continue to be concerned about the caps applicable to the reinsurers' retrospective tax and the tax rates which will be revised to generate the new revenue targets and to reflect the modifications to the tax base and new information that has recently become available. We hope that the insurers' and reinsurers' concerns will be addressed. Of course, the proposed caps on amounts collected from the various taxes should also relieve some of the concern over the tax rates.

We believe that passing the Superfund reauthorization legislation this year is crucial. This financing proposal constitutes the missing piece necessary to complete the Superfund reform puzzle. We would encourage the Committee to keep in mind the significant benefits to the country from the reform provisions and not let the financing of the EIRF become an obstacle.

Mr. Chairman, thank you for the opportunity to address this Committee. I will be pleased to answer any questions you or other members of the Committee may have.

RESPONSES OF LES SAMUELS TO A QUESTION FROM SENATOR BOREN

Question: Some of the criticisms of the current Superfund program are that hazardous waste site cleanups cost too much, take too long, and money better spent on cleanups is instead spent on legal fees to determine liability. Many of the provisions of S. 1834 are improvements over current law. I endorse the goals of making cleanups faster;' fairer and less costly.

However, there are several provisions of S. 1834 that could be seen as contrary to those goals. This bill allows the Environmental Protection Agency to increase the number of sites placed on the National Priorities List. This bill requires that all Superfund sites be cleaned up to a more stringent level over current levels. This bill gives states the flexibility to increase the standards used for cleanup above and beyond the federal standards. This bill exempts or limits the liability of municipalities and others who would have been liable under the current law.

Although many of these changes seem reasonable at first glance, they could result in higher cost cleanups at more sites with fewer responsible parties paying the tab. If this scenario came true, the federal government's financial obligations through the Superfund Trust Fund could increase.

I have seen several estimates on this bill's effect on the private sector but very little data on the effect of this bill on the Superfund Trust Fund—which I understand has a $2 billion surplus.

Has Treasury, EPA, or the Office of Management and Budget completed any estimates on the expected outlays for the Trust Fund? What are those estimates? Is it anticipated that the Trust Fund will need to be increased?

Answer: According to the Environmental Protection Agency, S. 1834 does not establish more stringent cleanup levels than current law. Rather, it establishes a clear national goal for cleanups that requires consideration of costs, technical feasibility, and future land use in making site-specific cleanup determinations. Further, the bill retains applicable cleanup standards and eliminates relevant and appropriate cleanup requirements, thereby significantly reducing the number of state standards that would apply to Superfund cleanups. These reforms, combined with the elimination of the statutory preferences for permanence and treatment in selecting remedies, should significantly reduce cleanup costs. The Administration conducted an extensive analysis of the Superfund Reform Act when it was introduced in February 1994, and concluded that the proposed reforms would reduce cleanup costs for all parties by 19% to 25%.

The liability reforms contained in S. 1834, particularly the exemptions from liability and the liability caps, are designed to increase the fairness of Superfund's liability scheme by getting the "little guy" out of the system. Although some of these reforms are expected to increase government's costs, they will substantially reduce transaction cost and virtually eliminate contribution actions.

The Administration's analysis of the bill as introduced concluded that the proposed reforms could be accomplished by extending at current levels the dedicated taxes that currently provide monies to the Superfund. The Administration's analysis estimated outlays of approximately $1.9 billion per year, on average, under the Superfund Reform Act.

PREPARED STATEMENT OF RICHARD D. SMITH

INTRODUCTION

My name is Richard D. Smith and I am President of The Chubb Corporation. I am presenting this testimony on behalf of the American Insurance Association ("AIA"). The AIA is a trade association comprised of 270 insurance companies, which together write a large portion of the commercial property and casualty insurance coverage which would be taxed to finance the Environmental Insurance Resolution Fund ("EIRF"). AIA and its member companies are intimately familiar with the impact of Superfund on business in general and on the insurance industry. in particular.

AIA supports reauthorization of Superfund this year. AIA also supports establishment of the EIRF as set forth in Title VIII of S. 1834. AIA also strongly supports the compromise proposal for financing the EIRF which was adopted by the House Ways and Means Committee in August.

BACKGROUND

In 1980, Congress enacted the Comprehensive Environmental Response Compensation and Liability Act, commonly referred to as Superfund. Superfund was intended to address a growing public concern: the cleanup of old hazardous waste sites, many of them inactive or abandoned years ago. Superfund uses an unprecedented retroactive, strict, joint and several liability system to force potentially responsible parties ("PRPs") to pay for these cleanups. Under this liability system, anyone who has ever had any connection with a hazardous waste site is held liable for the cleanup, including past and present owners of the property (even when the owner didn't know about the waste); the generators and transporters of the waste;

and anyone who arranged for the transportation and disposal of the waste. This liability dragnet, combined with the enormous cost of cleaning up Superfund sites, has led to extensive litigation at virtually every stage in the process.

For the insurance industry, this has meant even more litigation. As PRPs are notified of their potential liability or are assessed their share of the cleanup costs, many have claimed that hazardous waste liability is covered under their old insurance policies in effect at the time the waste was placed at the site. Insurers argue that these old policies were never intended to cover Superfund cleanup. These PRP lawsuits, however, result in time-consuming, expensive insurance coverage litigation that forces PRPs and insurers to spend additional money on more lawyers and consultants.

All levels of the state and federal judicial system are currently occupied in the interpretation of these insurance policies. There are a number of specific issues of contention which make this litigation extremely complex. Most legal experts believe it will take many years for all of the issues involved in the coverage litigation to be resolved. Moreover, even after all of the legal issues presented by the coverage litigation are resolved, we will still be litigating for years over the application of the facts in each case.

How much money is wasted on insurance-related transaction costs? Transaction cost information for the private sector has been difficult to assemble, largely because of the diverse number of parties, and the lack of site-specific accounting. In the most authoritative study so far, a 1992 study by Rand, it was reported that average transaction costs associated with insurance claims paid under Superfund were 88 percent of total costs. Even on closed claims, transaction costs averaged 69 percent, more than double the average for other general liability claims. Rand found that insurer transaction costs were running at $400 million per year for all waste cleanup claims. Transaction cost expenditures for PRPs must be at least equal to that figure.

The bottom line is this: the insurance coverage litigation will continue to result in hundreds of millions of dollars in unproductive, wasteful expenditures for years to come unless serious reform is adopted during this reauthorization of Superfund.

THE ENVIRONMENTAL INSURANCE RESOLUTION FUND

Title VIII of S. 1834 is intended to substantially reduce these transaction costs by establishing a unique system for resolving the insurance coverage disputes between insurers and PRPs. The EIRF is the product of a carefully negotiated compromise developed by insurers and PRPs working with the Administration.

The EIRF is intended to promote settlement of claims between insurance companies and PRPs. While the EIRF is not a complete solution, it is a constructive step toward limiting the unproductive and costly litigation which has pervaded the Superfund cleanup effort. In turn, it would channel funds to the companies financing the actual cleanup of Superfund sites.

FINANCING THE EIRF

The EIRF financing mechanism supported by the Administration and adopted by the House Ways and Means Committee reflects an extraordinary compromise among divergent interest groups. It would raise $8.1 billion over 10 years to pay for EIRF activities. Significantly, all of this revenue would come from the insurance industry and it would be the sole method of financing EIRF activities.

This compromise was not reached without pain. The Administration's original financing proposal called for 70% of the EIRF to be funded by a fee imposed on commercial premiums written from 1971 through 1985 (a retrospective element). The remaining 30% would have come from a prospective tax on commercial premiums.[1]

A great deal of debate ensued over the proper construct of the tax, particularly on the issue of whether the tax should be retrospective or prospective. A majority of AIA argued strenuously for a 100% prospective tax. The American International Group ("AIG") argued just as vehemently for a 100% retrospective tax. The coalition represented by the Chubb, which split from the AIA's Superfund Improvement Project, argued for a compromise along the lines proposed by the Administration.[2] After a great deal of difficult negotiation, the approach adopted by the Ways and

[1] See Statement of Leslie B. Samuels, Assistant Secretary (Tax Policy) Department of Treasury, House Ways and Means Committee Hearings on H.R. 3800, July 25, 1994, at 5.

[2] See Testimony of John P. Mascotte, American Insurance Association, Ways and Means Committee Hearings on H.R. 3800, July 25, 1994; Testimony of Maurice R. Greenberg, American International Group, Inc., Ways and Means Committee Hearings on H.R. 3800, July 25, 1994; Testimony of Richard D. Smith, Coalition for a Sound Insurance Resolution Fund, Ways and Means Committee Hearings on H.R. 3800.

Means Committee and supported by the Administration was developed. Accordingly, the Chubb coalition, along with AIG and the remainder of the AIA, together comprising approximately 50% of the property casualty insurance industry, strongly support the compromise reflected in the Ways and Means amendment.

That compromise can be summarized as follows:

- The EIRF is intended to total $8.1 billion over 10 years, funded at the rate of $810 million per year. The EIRF would be financed by two new excise taxes, one retrospective, one prospective and two special assessments. The retrospective tax would be based on commercial multi-peril and other liability premiums collected on policies issued between 1968 through the end of 1985, applicable to both insurance and reinsurance. The prospective tax would be imposed on a variety of commercial lines premiums collected after enactment. One special assessment would be on primary insurers beginning in 1999 and would be based on policies used in EIRF settlements. The other special assessment, also beginning in 1999, would be imposed on reinsurance coverage subject to EIRF settlements.
- During the first four years, 70% of the funding would be retrospective and 30% prospective. During the remaining six years, 65% of the funding would come from the prospective tax and the remainder would come from continuation of the retrospective tax on a portion of the reinsurance base and the special assessments applicable to both reinsurers and primary companies.
- Overall, 25% of the funding, or $200 million per year, would come from the reinsurance base. Of this, beginning in 1999, $167 million per year would come from a special assessment on reinsurance.[3]

THE REINSURANCE SHARE

The reinsurance industry has consistently stated that it is willing to pay its fair share of EIRF financing. The 25% share supported by the Administration and adopted by Ways and Means is a fair assessment. This allocation reflects the fact that although reinsurers take a smaller share of the premium on a given risk, they face a much higher risk exposure. For example, commercial multi-peril and other liability risks during the period 1968 through 1985 commonly were insured on an "excess of loss" basis.[4] Thus the primary insurers retain a certain amount of the risk while "laying off" higher levels to reinsurers. Because reinsurance covers higher levels of loss, reinsurance claims are less frequent than those at the primary level. However, when large losses do occur, they impose a heavier burden on the reinsurance sector. In covering large, but infrequent losses, reinsurers assume more exposure relative to each dollar of premiums than do primary insurers. A reinsurer might assume three times as much loss per dollar of premiums as would the primary insurers.[5]

Concerning the lines in the EIRF's financing, these risks commonly were layered with retentions held on various levels by the primary insurers. The average amount of reinsurance ceded for these risks during the relevant period was approximately 50%. The risk normally would be reinsured at 70% on the first level, 50% on the second level and 90% on the third level. Coverage ranged from five hundred thousand dollars to five million dollars during the early years. In later years, these types of risks would normally go up to the forty million dollar range with insurers accepting up to 99% of the excess twenty million dollars over the first twenty million.

Not surprisingly, financial analysts have expressed the opinion that reinsurers face greater exposure to Superfund liabilities than the primary sector. Earlier this year, the insurance rating firm, A.M. Best Co., released a study of property/casualty insurance environmental and asbestos liability exposures. The report states that "the uncertainty associated with environmental/asbestos exposures is significantly greater for reinsurers than primary companies . . . because of the higher policy limits and smaller premium amounts that reinsurers assume on any given . . . reinsurance program."[6]

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[3] See Explanation of Financing, H. Rept. 103-582, Part 3, House Ways and Means Report on H.R. 3800, Superfund Reform Act of 1994, at 19-29.

[4] Reinsurance is the "insurance of insurance." It is an important means of sharing risks among two or more insurance companies. In a typical reinsurance "excess of loss" contract a "primary" (or direct) insurer contracts for coverage with the policyholder and retains financial responsibility for losses below a specified threshold, reinsurance helps the primary company spread the risk of large losses to other insurers.

[5] Gerathewohl, *Reinsurance Principles and Practice*, Vol. I (1980) at 67-69.

[6] Snyder and Smith, "Environmental/Asbestos: The Industry's Black Hole," *Best's Review*, April 1994 at 102.

Reinsurers themselves believe that their pollution liability exposure far exceeds their premium market share. In 1985, the National Association of Insurance Commissioners convened an Advisory Committee on Environmental Insurance, which included reinsurance industry representatives. The Committee's 1986 report clearly stated the reinsurers' own concerns about pollution liability exposure: "Reinsurers are fearful that, although they represent only 10% of total property and casualty premiums and surplus, they may assume more than one-half of total pollution liability."[7]

Despite the enormous amount of reinsurance placed, the reinsurers argue that they have relatively little exposure. They assert that since the coverages were typically on an "occurrence" basis, each individual leak or dump at a given site constitutes an "occurrence" and thus their liability levels would rarely be triggered.

However, arguments based on what constitutes an "occurrence," depending on the primary coverage, are made a number of ways. For example, where there are no aggregate limits, a primary insurer would argue that the dump site itself constitutes a single occurrence for purposes of achieving its limit one time rather than many times, through each leak or dump. To our knowledge no precedent exists holding that each leak or dump is an "occurrence." In fact, Title VIII itself legislatively concludes that each site constitutes an occurrence. The average clean-up cost estimate per site is $28 million. Given the construct of reinsurance agreements in the relevant lines prior to 1986, the reinsurers' share could be a very large percentage if Superfund litigation were to run its course adversely to the insurance industry. Reinsurance arrangements generally obligate the reinsurer to "follow the fortunes" of the primary insurer, meaning that the reinsurer is bound to all legal interpretations of the underlying policy. Although primary insurers and reinsurers firmly maintain that their policies are not intended to cover Superfund clean-up, adverse judicial decisions holding such coverage exists are now and would continue to be binding on both insurers and reinsurers.

These legalistic distinctions aside, however, one constant remains: significant amounts of money are wasted in Superfund coverage litigation. Without the kind of reform reflected in the EIRF these issues will be litigated and arbitrated not only at the primary insurance level, but at the reinsurance levels as well. Arguing these issues on the various insurance and reinsurance levels will compound the waste of time and money created by Superfund.

The purpose of the EIRF is to end this waste and apply resources to clean-up through a reasonable contribution from the insurance industry in return for an end to litigation. The reinsurers, just as the primary companies, must realize that compromise is in order. In negotiating the EIRF, we realize that we may win some cases and we may lose others. Thus, the EIRF construct reflects compromise among competing legal arguments. Similarly, the reinsurers must realize that although they may not lose all of their cases and end up contributing 50-90% of any potential liability that might be determined, they likely are not going to win all their cases either. Given the uncertainty, the expense of litigation, and the potential exposure, the 25% contribution is a fair compromise.

EVEN WHEN MEASURED BY PREMIUM VOLUME, THE 25 PERCENT REINSURANCE SHARE IS FAIR

The 25 percent share for the reinsurers reflects the reinsurers' share of the premiums received during the period of 1968 through 1985. The reinsurers' premiums constitute 21% of the total relevant market. This conclusion is based on public data provided by A.M. Best for the years 1968 through 1985 in the relevant commercial lines.

The percentage is calculated by subtracting the available numbers for the domestic primary insurers' worldwide net premium from U.S. direct premiums. Making adjustments for the foreign premium included in worldwide net premium results in a 21% share held by reinsurers. Approximately 9% of the total is attributable to domestic reinsurers and about 12% is foreign placed reinsurance premiums. Using the inflation factor in the Ways and Means amendment to restate the figures in 1985 dollars results in the reinsurers holding a 19% share.

A 3–4% cushion is fair. It takes into account several things. First, as pointed out, reinsurers face much higher exposure levels. Secondly, a cushion is required because of the number of reinsurer insolvencies during the mid-1980's. Not all those with the retrospective base are still in existence. Lastly, the cushion allows for some correction in case of loss of foreign revenue.

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[7] Report of the NAIC Advisory Committee on Environmental Liability Insurance, Sept. 1986 at V–4.

TECHNICAL MODIFICATIONS

While AIA supports the proposal adopted by House Ways and Means, we note there are several relatively technical issues that need to be resolved. These are discussed with specificity below.

SUNSET

The proposal adopted by House Ways and Means contains a provision which sunsets the EIRF tax after ten years. The Sunset provision should be eliminated to allow the EIRF to "run off" all pending claims at the end of the 10 years. Specifically, it is highly unlikely that all of the claims brought to the EIRF will have been paid in full at the end of ten years. If the EIRF were forced to default on the payment of claims at the end of the tenth year due to a lack of revenues, all of the insurance coverage litigation would be revived. In effect, the EIRF will have been a failure: the insurance industry will have paid $8.1 billion in taxes and still have to face the coverage litigation the EIRF was intended to resolve. Any run-off should, of course, be capped at $810 million per year. We expect that the Treasury Department would make recommendations in the ninth year concerning the structure of the taxes to effect the run-off.

We understand that the Administration supports the elimination of the sunset provision.

BORROWING AUTHORITY FOR THE EIRF

AIA recommends that a limited grant of borrowing authority be extended to the EIRF. We believe this borrowing authority is a necessary cash flow management tool to ensure that the obligations of the EIRF will be satisfied as they come due.

Moreover, we believe this borrowing authority is essential to encourage PRPs to accept EIRF settlement offers. In order for the EIRF to go into effect, at least 85 percent of potential claimants must agree to accept the EIRF offer. In order to achieve this 85 percent acceptance level, it will be necessary to demonstrate that funds will be available as EIRF obligations come due. We are concerned that in the absence of borrowing authority, the 85 percent threshold will not be achieved. If this occurs, the EIRF will terminate.

We believe that the borrowing authority can be limited and structured in a way that guarantees that the borrowing will be repaid in full. Thus, we propose the borrowing authority be granted under the following constraints:

- Total borrowing would be limited to $200 million at any point.
- Borrowing would be limited to the tax receipts anticipated from the EIRF tax for the succeeding 12-month period.

We believe that these limitations would effectively limit any potential repayment risk to the federal government associated with this borrowing authority, while at the same time ensuring that funds will be available. This is essential to give the PRPs the confidence that if they choose to participate in the EIRF their claims will be paid.

LINES OF BUSINESS SUBJECT TO THE TAX

As currently drafted, the proposal adopted by the Ways and Means Committee, contains a provision which gives the Secretary of the Treasury the discretion to change the lines of business which may be subject to the tax. AIA opposes this provision. This is a very broad grant of authority which, depending on how it is applied, could result in a major change in the way the EIRF tax is applied.

ANNUAL REVENUES SHOULD BE CAPPED

While AIA supports the EIRF tax mechanism adopted by the Ways and Means Committee, we believe that the tax rates written into that proposal are far too high and would generate revenues far in excess of the amount required for each year of EIRF operation. On the other hand, we agree that it is always difficult to compute tax rates which would be precisely accurate for any given year, since premium levels will no doubt vary. In fact, we believe premiums will grow substantially over the next 10 years, just as they have in the past.

To resolve this problem, we support imposing an annual cap on revenues for each segment of the tax. Once the cap is reached in any given year, no more tax would be collected until the following year. Using the formulas contained in the proposal adopted by Ways and Means, the caps would be as follows:

ANNUAL REVENUE CAPS

(Asterisk indicates special assessments)

Tax Years	Insurers Retro.	Insurers Prospect.	Reinsurers
1 to 4	$367.0M	$243.0M	$200.0M
5 to 10	$0	$526.5M *$81.0M	$200.0M

FAIRNESS OF THE TAX

Given this contour of the tax, a preliminary review by Standard and Poors indicates that the EIRF's financing will fall predominantly on 30 insurer groups. The majority of these are AIA members and others who support the EIRF.[8]

In sum, the EIRF financing mechanism adopted supported by the Administration and adopted by Ways and Means is fair and equitably tailored to place the burden on those who will benefit most.

CONCLUSION

AIA urges the Committee to adopt the EIRF financing mechanism in the form reported by the House Ways and Means Committee with the modifications suggested above.

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[8] Standard & Poor's Corp., *Credit Wire* (August 30, 1994).

STATEMENT OF
HOWARD E. STEINBERG
ON BEHALF OF THE
NATIONAL ASSOCIATION OF INDEPENDENT INSURERS
ON S. 1834
BEFORE THE SENATE FINANCE COMMITTEE
SEPTEMBER 14, 1994

Mr. Chairman, members of the Committee, the proposed Environmental Insurance Resolution Fund ("EIRF") was conceived for the purpose of achieving a worthy goal -- reducing litigation over Superfund coverage disputes. If properly implemented and funded, NAII would support it. Unfortunately, however, the funding methodology of Title IX of S. 1834, as approved by the House Ways and as Means Committee and currently before this Committee, is fundamentally flawed unfair and unworkable. It completely fails to meet the principles set forth by Treasury, including particularly the principle that those who benefit from the EIRF should provide most of the EIRF's funding. Instead, it would shift the burden of financing the EIRF from the insurance companies whose liabilities will be paid by the EIRF to competitors that have little or no environmental exposure and thus, receive little or no benefit from the EIRF. Consequently, in its present form, it is wholly unacceptable to the vast majority of property and casualty ("P&C") insurers.

NAII has proposed an alternative financing mechanism which is workable, fair and complies in every way with Treasury's guiding principles. The NAII proposal would replace the inequitable premium tax-based approach in the bill before you with two additional corporate environmental taxes, applicable only to certain property and casualty insurers. These taxes would be added on top of the existing CET under Section 59A of the Internal Revenue Code. This alternative would have very significant advantages over the current proposal, which relies primarily upon the imposition of new premium taxes to fund the EIRF. First, it more accurately and fairly allocates the tax burden to those who benefit from the EIRF; second, it builds upon an existing tax structure, avoiding the necessity of developing a new, complex tax scheme; third, it avoids a regressive federal "sales" tax on insurance products; and finally, it does not involve the imposition of retrospective taxes.

Good afternoon. My name is Howard E. Steinberg, Senior Vice President and General Counsel of Reliance Group Holdings, Inc., the parent company of Reliance Insurance Company. Reliance Insurance Company has conducted business since 1817, making it one of the oldest property and casualty insurance companies in the United States. Reliance Insurance is headquartered in Philadelphia and operates in all 50 states and the District of Columbia. It writes primarily standard commercial business through more than 3,000 independent agents as well as regional and national brokers. Reliance Insurance is ranked by A.M. Best as the 19th largest insurance company based on direct premiums written.

I am appearing here today on behalf of the National Association of Independent Insurers ("NAII"), an organization consisting of 575 independent insurance companies of which Reliance Insurance is a member. I have also been authorized to state the position of NAMIC, the National Association of Mutual Insurance Companies ("NAMIC"), which has over 1200 member companies. Accompanying me is Jack Ramirez, Executive Vice President and Chief Operating Officer of NAII.

We strongly believe that the current provisions of Title IX of S. 1834 related to the financing of the EIRF must be substantially amended because they are severely flawed, unfair and

unworkable as currently written. NAII specifically opposes the efforts of a few very large P&C insurers that wrote the vast majority of policies resulting in disputes over environmental cleanup coverage to shift a substantial portion, if not the majority, of the burden for settling their private insurance claims onto other insurers that are not exposed to direct and actual liability for such claims.

The bill currently before this Committee continues to rely, as the Administration's original proposal had done, primarily upon the imposition of a system of new retrospective and prospective premium taxes to fund the EIRF. The current proposal, however, actually exacerbates the unfairness and infirmities of the Administration's original proposal by altering the relative rates and scope of these taxes.

In its present form the bill would, in years 1 through 4, raise 30 percent of the funds for the EIRF from a prospective premium tax on virtually all commercial insurance premiums, 45 percent from a retrospective premium tax on certain commercial premiums of direct insurers written during the period of 1968-1985, and 25 percent from a retrospective tax on reinsurance premiums with respect to such commercial insurance. In years 5 through 10, the current bill would raise 65 percent of the funding from an increased prospective premium tax, 4.4 percent from continuing the retrospective tax on reinsurance at a lower rate, 10 percent from special assessments on direct insurers having claims resolved by the EIRF, and 20.6 percent from direct assessments on reinsurers having claims resolved by the EIRF. A total of $8.1 billion dollars ($810 million per year) will be raised from these sources as follows:

	Prospective Premium Tax	Direct Insurer Retrospective Premium Tax	Reinsurer Retrospective Premium Tax	Direct Insurer Special Assessment	Reinsurer Special Assessment
Year 1	$243,000,000	$324,000,000	$202,500,000	$0	$0
Year 2	$243,000,000	$324,000,000	$202,500,000	$0	$0
Year 3	$243,000,000	$324,000,000	$202,500,000	$0	$0
Year 4	$243,000,000	$324,000,000	$202,500,000	$0	$0
Year 5	$526,500,000	$0	$35,500,000	$81,000,000	$167,000,000
Year 6	$526,500,000	$0	$35,500,000	$81,000,000	$167,000,000
Year 7	$526,500,000	$0	$35,500,000	$81,000,000	$167,000,000
Year 8	$526,500,000	$0	$35,500,000	$81,000,000	$167,000,000
Year 9	$526,500,000	$0	$35,500,000	$81,000,000	$167,000,000
Year 10	$526,500,000	$0	$35,500,000	$81,000,000	$167,000,000

Although the EIRF and its proposed financing mechanism have been characterized by the Administration as a compromise for resolving pending litigation, the compromise negotiations have involved representatives of only a small minority of P&C insurers and reinsurers, whether measured in terms of number of companies or premium volume.[1] The resulting proposal does not represent a compromise widely supported in the P&C industry. To the contrary, it is opposed by the overwhelming majority of P&C insurers as representing an attempt by a few large, primarily east coast insurance companies to shift their environmental liability to the rest of the industry. In short, it is only a "compromise" between the Administration and this small group of large insurers, principally those represented by the American Insurance Association (the "AIA"), the American International Group ("AIG") and Lloyd's of London.

Moreover, the process by which the negotiations leading up to the current proposal were conducted amply demonstrates that the current proposal is not a true "compromise" by the P&C

[1]The AIA represents 50 P&C insurance companies which account for approximately 22.9 percent of the industry's net written premiums. AIA does not represent -- nor can it purport to speak on behalf of -- the vast majority of P&C insurers.

insurance industry as the Administration has attempted to characterize it. Many of the major insurance associations were not even invited to participate, and it was made clear from the outset to those that were that AIA would have veto power over any proposal. Under such circumstances, it is not surprising that no serious consideration was given to other proposals, such as that offered by the NAII, or that the end product of these "compromise" negotiations was a proposal through which AIA, AIG and those supporting the Administration managed to carve out an even bigger benefit for themselves than under the original proposal.

In the final analysis, the "compromise" reached by these parties and the Administration, which is now before this Committee, represents a "disguised bail-out" of certain large commercial P&C insurers. In actuality, these few large insurers are having liabilities against them settled by paying pennies on the dollar. They receive this benefit at the expense of the many insurers who were not given a real voice in the "compromise" process.

Furthermore, an examination of the changes from the original proposal makes it inescapably clear that the current proposal is nothing more than an attempt to "buy off" those insurers who have agreed to switch to supporting the Administration. AIG, for example, received a tremendous windfall in that it was able to obtain the Administration's and AIA's backing to exclude premiums on two of its primary lines of business -- directors and officers and other professional liability insurance -- from the extremely broad definition of commercial insurance subject to the prospective premium tax. Similarly, the acquiescence of those members of the AIA that had been objecting to the original Administration proposal on the grounds that it should be imposed entirely prospectively was obtained by dramatically increasing the prospective tax burden. Finally, the so-called "concession" made to P&C insurers with little or no environmental liability is in reality a meaningless gesture -- the $5 million floor on commercial premiums, while characterized as a "benefit" to small insurers in actuality represents an amount of commercial premiums so small as to be virtually inconsequential to more than a very, very few insurers. In fact, any good commercial insurance *agent* has this much premium volume in a given year.

In the end, the result of this so-called "compromise" is a proposal that would introduce an unwise and unfair tax regime for the vast majority of insurance companies and which fails to meet the Administration's own objectives for funding the EIRF.

The proposal violates the fundamental principles that the Treasury established as appropriate criteria for any EIRF funding source.

In the testimony and statement of Leslie B. Samuels, Assistant Secretary (Tax Policy), given before the House Ways and Means Committee on July 25, 1994, the Treasury identified three fundamental objectives that any taxes to be used in funding the EIRF should meet. These objectives were that the tax:

(1) ensure that the "insurers that benefit from the environmental insurance resolution reform -- those that have potential Superfund liabilities through commercial insurance coverage written in the past -- should provide most of the EIRF's funding";

(2) reflect that the "commercial insurance industry as a whole, its policyholders, and society also will benefit from the reform and should pay some portion of the EIRF's funding"; and

(3) recognize that "commercial insurers and reinsurers, whether domestic or foreign, that insure risks in the United States benefit from the reform and should participate in its funding."

The bill in its current form, like the Administration's original proposal, fails to achieve *any* of these objectives and indeed is worse in many respects than the original proposal.

Those That Benefit From the EIRF Do Not Bear Their Fair Share of the Burden. In considering the EIRF financing provisions, Congress should be mindful of the fact that the proposed EIRF is in essence a statutory mechanism for settling private insurance claims against certain P&C insurers. Not all insurers have Superfund coverage claims, and of those that do, the amounts of the claims vary considerably. Approximately 30 (out of the more than 3,000 P&C insurance companies) have more than 75 percent of the claims. These 30 companies will be the primary beneficiaries of the EIRF as a result of having claims against them settled by the fund. These companies will save the enormous costs that would otherwise be incurred in litigating these claims, and will see their balance sheets and their competitive position in the marketplace dramatically improved.

In fact, the current proposal actually shifts a substantially greater proportion of the burden for financing the EIRF onto insurers that have little exposure to claims for environmental clean-up costs. Under the original proposal, commercial insurers subject to the prospective tax would have provided $2.43 billion of the total funding for the EIRF. Under the current bill, they would now be called upon to pay over $4.13 billion.

Moreover, the definition of commercial insurance subject to the prospective premium tax has been grossly overexpanded from the original proposal to now encompass fire (with certain exclusions for residential housing coverage), commercial multiple peril, other liability, product liability, allied lines, inland marine, commercial auto no-fault, other commercial auto liability, commercial auto physical damage, farm owners multiple peril, ocean marine, financial guaranty, aircraft, fidelity, surety, glass, burglary and theft, boiler and machinery, <u>and other lines designated by the Secretary.</u>[3] Thus, the revised proposal would place the burden of the prospective tax upon a vastly larger group of P&C insurers.

Treasury has given no explanation of the rationale for expanding the scope of the prospective tax to sweep in more lines of business that have no possible connection to the coverage of environmental clean-up costs. The only effect is to ensure that even more P&C insurers with little or no environmental clean-up liabilities are forced to help finance a "disguised bail-out" of a portion of the P&C industry. It is difficult to see the justification behind imposing a tax that essentially requires small insurance companies to subsidize a few large, P&C insurers in this way.

Similarly, the revised proposal shifts a larger portion of the burden for financing the EIRF onto reinsurers. The revised proposal increases the share of the retrospective tax burden of these reinsurers from 6.2 percent to 12.6 percent, increasing the amount of taxes imposed upon such companies by $522 million.

While the goal of reducing litigation over Superfund coverage disputes in an expeditious and efficient manner is laudable, and NAII supports that goal, considerations of equity require that any financing mechanism proposed for the purposes of funding the EIRF should place the EIRF's costs upon those companies that will benefit from its operation. As shown above, however, the bill's current proposal for financing the EIRF fails miserably in achieving this goal. To the contrary, the revised proposal would shift approximately an *additional $2.2 billion* from those directly benefiting

[3]Premiums subject to this tax under the original proposal would generally be those with respect to commercial policies, including commercial multi-peril policies and other liability policies, with certain exceptions for non-commercial policies or other policies that provide neither comprehensive general liability coverage nor environmental liability coverage.

from the EIRF onto other insurers. This represents nothing more than a thinly disguised and unjustifiable subsidy of a handful of large insurance companies at the expense of the rest of the industry. Such an intrusion of the government into the free operation of the economy is totally unwarranted and objectionable.

It is patently unfair, inherently in conflict with the nature of the EIRF, and squarely at odds with the first fundamental principle articulated by Treasury. We therefore urge this Committee to seriously consider whether it is appropriate to place *any* of the financing burden -- in whatever fashion imposed -- upon insurers other than those commercial P&C insurers whose claims are actually being resolved by the EIRF.

Nevertheless, if this Committee should conclude that some portion of the burden for claims settlement should be apportioned to insurers without direct liability in order somehow to reflect a "societal" benefit from the EIRF, the financing approach that I will present today represents a more equitable and administratively efficient method for doing so than would be the case under the current bill.

The Financing Proposal Fails to Accurately Represent Any "Benefit" To Society At Large. Even accepting that the EIRF would benefit society as a whole, and not just those insurers and reinsurers having environmental coverage claims against them resolved thereby, the current proposal fails to accurately reflect such potential benefit. In its original proposal, the Treasury advocated a premium tax structure that would have placed approximately 30 percent of the cost of the EIRF upon those P&C insurers currently writing the lines of commercial business that are of the same type that gave rise to environmental clean-up coverage disputes. The Treasury justified this tax on the grounds that it reflected the benefit to society and to the P&C insurance industry in general.

The current proposal would dramatically increase the tax burden imposed upon "society at large" by increasing prospective premium tax rates and expanding the definition of commercial insurance. If the Administration's prior proposal represented a "fair" estimate of the apportionment of the burdens of financing the EIRF based upon the benefit to society, then clearly the current proposal places an excessive and unfair burden upon society. If Treasury is now saying that its revised proposal is a fair and accurate estimate of the benefit to society and the P&C industry as a whole, then the question must be asked why Treasury has decided that this benefit is substantially larger than originally estimated.

In any event, Congress should hardly be called upon to blindly "trust" the Treasury's judgment in these matters, especially when the Treasury seems to be arbitrarily imposing a tax burden on insurers with little or no exposure to Superfund liability claims and indirectly to the whole of society. The Treasury should be called upon to specifically justify and prove its estimates of the "benefit" received by society and other insurers before a substantial portion of the costs are shifted off of those insurers directly benefiting from the EIRF.

The Financing Proposal Potentially Imposes a Burden Upon Personal Lines of Insurance. It is not clear that the prospective premium taxes will be able to be passed on fully to commercial insureds. Consequently, P&C insurers may be forced to attempt to spread the prospective tax across personal lines as well, i.e., home owners insurance and private automobile insurance.

The Financing Proposal Potentially Imposes Disproportionate Burdens Upon Domestic and Foreign Insurers. The revised proposal allows foreign insurers not otherwise subject to U.S. income taxation to avoid being subject to the prospective premium tax. Foreign insurers or reinsurers not doing business in the United States, which nevertheless insure U.S.-source risks, are not subject to the retrospective premium taxes, prospective premium taxes, or special assessment

fees. Instead, those insurers are made subject to a special 0.5% tax on their maximum limits of liability on all commercial insurance of U.S. source risks. They are able to elect out of this tax by agreeing to pay just the retrospective tax (and presumably the special assessments) imposed on domestic direct insurers and reinsurers.

However, domestic direct insurers and foreign direct insurers subject to U.S. income taxation are also required to pay prospective premium taxes. Foreign insurers not subject to U.S. income taxation appear to avoid any tax liability under the prospective premium tax. This potentially confers an unfair competitive advantage upon some foreign competitors of U.S. insurers.

Federal premium taxes are an unfair and inappropriate method for funding the EIRF.

Any scheme to fund the EIRF by use of a federal premium tax would be fraught with problems and serious implications. This Committee should not embark on any such new federal taxing scheme without first closely reviewing and considering those problems and implications. The premium tax proposal before this Committee is particularly ill conceived and objectionable.

As noted above, the proposed tax scheme would utterly fail to place an equitable burden on those P&C insurers that would benefit from the resolution of claims regarding the coverage of Superfund cleanup costs. The prospective tax component of the current bill will be assessed on premiums written by insurance companies that may not be exposed to significant liability claims under Superfund. In fact, many of the companies that would be subject to the tax had little or no commercial liability business of any kind during the years covered by the disputed claims. Nevertheless, virtually all P&C insurance companies would be assessed a premium tax to settle claims involving only a small portion of the industry. Moreover, the current proposal worsens this situation by grossly over-expanding the definition of commercial insurance to sweep in lines without even a tangential connection to those types of policies that have given rise to suits for environmental clean-up cost coverage, e.g. commercial auto, financial guaranty, burglary and theft and farm owner's multiple peril insurance.

In the case of the retrospective tax component, a tax assessed with respect to certain commercial liability policies written during the years 1968 through 1985, the tax fails to draw distinctions between insurance companies having substantial exposure to environmental clean-up claims under policies written during that period and companies having little or no exposure to such claims. The retrospective component of the premium tax is a very blunt instrument that, comparing potential litigation costs with potential tax liabilities, would result in a few large companies being big "winners" and would result in many smaller and emerging companies becoming big "losers."

Reliance Insurance is an excellent example of how draconian the proposed premium tax would be. As currently proposed, 45 percent of the tax in years 1 through 4 would be based upon commercial premiums written during the 18 years from 1968 through 1985. During this period of time, Reliance Insurance wrote commercial insurance policies principally for small and medium sized businesses. We liked to think of our typical customer as a hardware store in Middle America. Consequently, Reliance Insurance has very little exposure for environmental coverages during that period. Out of total loss reserves of nearly $3 billion, we estimate that, on a worst case basis, only approximately $30 million or 1 percent, are attributable to Superfund claims. Our estimates of future legal expenses for declaratory judgment actions involving Superfund sites is under $3 million dollars. Nevertheless, we estimate that the proposed premium tax could cost us as much as $135 million over the next 10 years. That would be $135 million of additional tax with virtually no benefit to us. It is, of course, an understatement to say that we regard this as grossly unfair.

Even among P&C insurers with actual claims exposure, the currently proposed premium tax provision may prove grossly inequitable and result in significant economic distortions. Since not all persons with claims against insurers for environmental clean-up costs must accept participation for the EIRF to go into effect, it is possible that an individual P&C insurer with direct exposure may have a significant tax burden imposed upon it, and yet receive no benefit thereby if its particular insureds choose not to accept settlements.

Furthermore, the proposed "special assessments" to be paid in years 5 through 10 by direct insurers and reinsurers having claims resolved by the EIRF hardly remedy any of these inequities by placing less than 18.4 percent of the total financing burden onto such companies.

The proposed new federal premium tax scheme raise profound federalism concerns.

The proposed EIRF premium taxing scheme would encroach upon a tax base that has been historically reserved to the states. In 1991, for example, the various states collected approximately $7.7 billion in premium taxes, generally in lieu of state and local income taxes on insurance companies. As in the case of proposals for general national sales taxes, the federal premium tax proposal places the federal government in competition with states for a common tax base.

Potential conflicts among states taxes have been addressed through retaliatory tax provisions in the various states. Under these provisions, a state seeking to impose a high rate of premium tax on insurers doing business in that state, but domiciled in another state, faces the prospect of triggering a retaliatory increase in premium tax by the domiciliary state with respect to insurers domiciled in the first state and doing business in the second state. Because of these retaliatory provisions, there is some constraint on increasing premium tax rates at the state level. However, a premium tax on the federal level, once instituted, would not be subject to this inter-jurisdictional tax constraint. As in the case of proposals for general national sales taxes, the federal premium tax proposal creates the potential for crowding out the states.

The proposed new federal premium taxes are regressive.

Like other sales taxes, the proposed premium taxes would be regressive. They are not based on ability to pay. Because the tax would essentially be imposed on gross income, rather than net income, a P&C insurer would have substantial federal premium tax liability even if it had an economic loss from operations, and negative taxable income, for the taxable year. The taxes therefore impose a regressive burden on those who bear it economically, since the taxes are largely unrelated to a company's ability to pay.

The proposed EIRF federal premium tax incurs unnecessary and substantial administrative costs.

The current proposal would create an entirely new tax, with new compliance burdens on insurance companies and new enforcement burdens on the Internal Revenue Service. Although the concept of a premium tax may seem simple, implementation would involve numerous complications. The proposal would introduce such newly defined terms as: applicable funding rate, applicable target revenue amounts, assessable person, adjusted base-period commercial premiums, inflation-adjusted commercial premiums, inflation adjustment factor, exemption amount (with aggregation rules), commercial net premiums, qualified commercial policies, allocated reinsurance, unallocated reinsurance, commercial reinsurance share, taxable period, base period, base-period year, direct premiums written, net premiums written, annual statement, policy, foreign person, policy of casualty insurance, related person, and maximum limit of liability.

Perhaps the complexities resulting from the creation of this new taxing structure could be tolerated if the proposal represented sound substantive tax policy. But, in this case, the complications serve instead to compound the problems associated with its substance.

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The proposed EIRF federal premium tax imposes a substantial new tax burden on insurance companies.

The aforementioned policy problems inherent in a federal premium tax, i.e., inequity, federalism, regressivity and complexity, cannot, moreover, simply be swept under the rug on the grounds that the proposal calls for taxes at a relatively low percentage rate (ranging from 0.33% to 0.63% of premiums with respect to the prospective tax). These percentages can be deceptive. Bear in mind that the tax is imposed on gross revenues (i.e., premiums), rather than net income. As a result, a premium tax at a given rate is comparable to a net income tax imposed at a rate many times higher than the premium tax rate.

Consider, for example, that the gross premiums written in 1992 for all P&C insurance lines totalled about $230 billion while the net income (determined for regulatory purposes) was approximately $10 billion. Using this 23:1 ratio, the 0.63% prospective premium tax applicable for years 5 through 10 is roughly comparable to a 15% tax on net income related to the policies in question. And the premium tax would be in addition to the regular federal income tax paid by P&C insurers. Viewed in this light, the proposed premium tax -- even if only the prospective portion is taken into account -- is of major significance.

The current proposal creates the possibility for budget mischief.

The revised proposal would make clear that the EIRF Trust Fund is "on budget." This creates the possibility for the Administration to engage in all kinds of creative and abusive budgetary accounting that thwarts the objective of deficit reduction. An example of precisely this type of potential abuse can be seen in the Administration's consideration of proposals to use the accounting surplus from the Superfund to "pay" for welfare reform.

NAII's proposal would raise the required EIRF financing, fulfill the principles enunciated by Treasury and avoid the problem of a new, untested Federal premium tax scheme.

The NAII, therefore, urges that the current proposal for financing the EIRF be replaced with a simple and easily administrable structure of Corporate Environmental Tax ("CET") taxes (applicable only to certain commercial P&C insurers -- both direct insurers and reinsurers) that can be added onto the existing CET provisions contained in Section 59A of the Internal Revenue Code without requiring the creation of a new and separate tax system. See Appendix A to this statement for a copy of the statutory language of this proposal, which has been attached for purposes of the Committee's records. While NAMIC opposes the EIRF and believes that it should be deleted at this time, if Congress feels compelled to go forward with the EIRF NAMIC would also support NAII's alternative. This CET tax structure would be less complicated, less costly to administer, and would more equitably allocate the burden of the EIRF to those P&C companies that currently face environmental clean-up exposure ("Exposed P&C Insurers"). The CET approach that the NAII proposes also fully meets the Administration's own criteria for an acceptable funding mechanism for the EIRF.

The first component of this structure would be a Commercial Insurer Tax upon those P&C insurers currently writing business in the commercial property and casualty insurance lines that are of the same general type as those contracts that gave rise to environmental clean-up costs claims, i.e., the other liability, commercial multi-peril and fire lines of business. The amount of the tax would be equal to the amount of Alternative Minimum Taxable Income used in computing the insurer's general Corporate Environmental Tax under section 59A of the Code multiplied by the Commercial Insurer Tax Rate multiplied by the percentage of such business written by each individual insurer. The Commercial Insurer Tax is designed to generate the same amount of revenue as would have been raised by the prospective premium tax in the Administration's original proposal (approximately 30 percent of the total), but to do so in a manner that is more equitable and less costly to administer than the proposal in Title IX.

The second component of the NAII's proposed structure would be a Claims Settlement Tax imposed only upon those P&C insurers with actual environmental cleanup cost claims that are being resolved by the EIRF. A total tax amount would be set for each year of the EIRF's operation. Each P&C insurer having claims resolved by the EIRF would then pay a tax equal to its proportional share of this amount (based upon the value of claims being settled as annually redetermined). Provision would also be made to adjust the amounts collected at the end of the 10-year period to reflect the actual amounts of claims resolved against each exposed P&C insurer. This tax is designed to raise the same amounts as would have been raised by the retrospective premium tax in the Administration's original proposal (approximately 70 percent of the total), but through a mechanism that would closely tie the amount of tax liability to the proportion of benefit actually being received.

As under present law, both of these taxes would apply regardless of whether a company is paying alternative minimum tax or regular income tax. These taxes are also both fully prospective, structured to cover both domestic and foreign insurers and reinsurers (with a separate 0.5 percent tax on maximum limits of liability to be imposed upon certain foreign insurers and reinsurers not subject to U.S. income taxation that do not elect to become subject to the CET taxes) and contain rules to relating to the treatment of insurance companies that are members of consolidated groups.

Commercial Insurer Tax

The Commercial Insurer Tax will be imposed upon those P&C insurers that write designated commercial lines of business, i.e., general commercial and commercial multi-peril, that either represent more than a de minimis percent of their total business, or represent more than $2 million of annual net premiums (in order to simplify administration). For these purposes, designated commercial insurance would specifically exclude any types of insurance, even if commercial in nature, that would not have given rise to environmental cleanup coverage claims, such as dwelling fire insurance.

For these purposes, each P&C Insurer writing designated commercial insurance will annually compute the percentage of its net premiums from designated commercial insurance to its total net premiums from all business (the "Designated Commercial Insurance Percentage"). This percentage will be determined from the most recent Annual Statement of each P&C insurer filed before January 1, 1995 for the first year in which the Commercial Insurer Tax is in effect, and shall be determined from succeeding Annual Statements for the years in which the tax remains in effect.

The Commercial Insurer Tax rate will be as follows for each year in the 10-year period beginning on the date on which the EIRF becomes effective (as determined pursuant to the provisions of Title VIII):

Year 1	5.727 %
Year 2	5.296 %
Year 3	6.734 %
Year 4	6.495 %
Year 5	6.112 %
Year 6	6.717 %
Year 7	7.265 %
Year 8	7.761 %
Year 9	8.209 %
Year 10	8.610 %

Each P&C insurer, subject to the Commercial Insurer Tax will multiply its alternative minimum taxable income ("AMTI") over $2,000,000 by the product of the Commercial Insurer Tax times the Designated Commercial Insurance Percentage to determine the amount of the Commercial Insurer Tax owed.

Claims Settlement Tax

Since the EIRF is in essence a government sponsored program to settle private litigation between the Exposed P&C Insurers and insureds that have claims for environmental cleanup costs, and since, moreover, these companies will benefit from a significant decrease in their transaction costs associated with handling and litigating such claims as the result of EIRF, it is appropriate for them to bear the vast majority, if not all, of the EIRF's costs (as the Treasury originally testified).

The Claims Settlement Tax would, however, successfully accomplishes this precise objective. Assuming that the effective date of the tax provisions for funding the EIRF is appropriately deferred until after the EIRF is determined to have become effective, then the EIRF Board will possess a considerable amount of information about the claims being resolved, permitting them to determine the relative amount of benefit that each insurer with claims for environmental clean-up costs will be receiving. The Claims Settlement Tax takes full advantage of this information in order to both specifically target the group of insurers who should pay the tax and fairly allocate the total tax burden within this group.

Mechanically, under this proposal, an additional tax (on top of the basic CET Tax and the Commercial Insurer Tax) would be imposed upon each Exposed P&C Insurer. Once the EIRF has become effective, it will be possible for the EIRF Board to make a specific estimate of the potential amount of claims (adjusted to settlement value under the provisions of Title VIII) against each Exposed P&C Insurer that the EIRF will resolve (the "Individual Company Resolution Amount"), and to make therefrom an estimate of the potential amount of claims (adjusted to settlement value) against all Exposed P&C Insurers to be resolved by the EIRF (the "Total Resolution Amount"). The EIRF Board will divide the Individual Company Resolution Amount by the Total Resolution Amount to compute the Company Resolution Percentage for each Exposed P&C Insurer, and shall transmit this percentage to each Exposed P&C Insurer.

For each year in the 10-year period beginning after the EIRF becomes effective, the amount of each Exposed P&C Insurer's Claims Settlement Tax will be determined by multiplying the annual Targeted Claims Settlement Tax Amount by their Company Resolution Percentage. The total Targeted Claims Settlement Tax Amount will be $5.67 billion over ten years, and will range from $350 million in year 1 to $840 million in year 10 (raising the same amount as the retrospective tax would have done under the original Administration proposal).

Caps on Commercial Insurer and Claims Settlement Taxes

In conjunction with the Commercial Insurer Tax and Claims Settlement Tax, a system of caps and credits should be installed to prevent the amount actually collected from exceeding the amount targeted to be raised. This is appropriate because these taxes are being collected for just a specific purpose, i.e., the EIRF.

Special Tax on Maximum Limits of Liability

A 0.5 percent tax, modeled on the administration's proposal, would be imposed on the maximum limits of liability of foreign insurers and reinsurers with respect to policies insuring U.S. source commercial risks if such insurers and reinsurers are not otherwise subject to the Commercial Insurer Tax and Claims Settlement Tax. This special tax may be avoided by entering into a closing agreement whereby the foreign insurer agrees to be made subject to these taxes.

Testimony of W. Larry Wallace, Executive Director of the Alliance for a Superfund Action Partnership (ASAP)

Presented Before the United States Senate Finance Committee

September 14, 1994

Good Morning. I am Larry Wallace, Executive Director of the Alliance for a Superfund Action Partnership (ASAP). I appreciate you inviting me here today to share with you ASAP's views of S.1834.

Today, ASAP represents the broadest and largest diverse constituency of Superfund stakeholders you can find: the NAACP, Local Governments for Superfund Reform, the American Furniture Manufacturers Association, the City of Atlanta, the Society of Independent Gas Marketers of America, the National Food Processors Association, The Grocery Manufacturers of America, Johnson Controls, Inc., Jesus People Against Pollution, Texaco, Phillips, and many others in a variety of fields. A full list of current membership will be submitted for the record.

At one time or another, everyone here has said that there's too much litigation in Superfund, too much mistrust, too little cleanup. And many have also agreed that a major cause of all these problems is the retroactive, site-by-site system used to raise cleanup funds.

Your Committee is being asked to continue more than a $1 billion a year in current taxes, and to raise hundreds of millions of dollars more in taxes. You are the checkwriters for this program -- you should therefore have confidence that the money is wisely spent.

Yet, you are here today seriously considering a bill drafted by the Administration which will keep this failed system in place. Moreover, the bill contains provisions that would further complicate the complicate the legal warfare and that would divert hundreds of millions of dollars that could be used for cleanup.

The Clinton Administration touts this bill as representing a "consensus" among Superfund stakeholders. However, I am here to tell otherwise. S. 1834 does not begin to represent the concerns and troubles of the thousands of affected parties residing beyond the Beltway. This bill, in the strictest sense, is a political agreement crafted by an exclusive group of players -- EPA and only a limited circle of Superfund stakeholders.

Theirs is a view glimpsed from Washington's corridors, not from toxic ground zero -- the communities and people living with Superfund risk every day. In Washington, the talk is of making "polluters" pay and of "fair share" allocation.

At toxic ground zero, the talk is of one thing: Clean up our neighborhood, do it fast and do it right. Communities want to see cleanup crews and public health professionals, not lawyers, allocators and allocation committees.

I encourage you to read S. 1834 very closely. After a thorough read of the bill, I am sure you will agree that not all stakeholders benefit from the bill or its financing priorities. The consensus of Superfund stakeholders supporting S.1834 grows even smaller when you begin to consider the bill's various provisions.

In order to garner support for the bill, the Administration has cut special deals with some favored business and municipal constituencies. The bill also buys off opposition from others with complicated compromises. But what it does not do is fundamentally reform Superfund to make it work to protect the citizens living near toxic waste sites.

Impact on Citizens Living Near Sites

Residents living in and around Superfund sites have an intense interest in the Superfund reform debate, but for the most part lack the formal organization to participate effectively in Washington. That will not be true when this so-called reform plan fails to achieve meaningful results, amounts spent on cleanup from the Trust Fund at sites without PRPs are cut, and a groundswell of public outrage lights up district message centers across the country.

As ex-EPA Administrator Bill Ruckelshaus recently noted, citizens who live near Superfund sites are among the most alienated Americans he has seen since the Vietnam War; "they don't think anyone cares." The Administration bill will not change that. Indeed, after this fierce reform debate, it may aggravate it.

Yet, S. 1834 says: "More than $1 billion in new commitments to reduce current PRP liability, but not a dime to increase cleanup spending."

Citizens are already angered by the lack of faster cleanup. Under HR 3800, they will continue to be. The bill's liability allocation provisions, even if they succeed, will not stop the legal battles over money. Indeed, they will increase PRPs' current incentives to delay cleanup and fight over the costs of remedies, by making such resistance cheaper. Citizens will be angered at the slowdown in cleanup at orphan sites, where there are no PRPs to pay for cleanup but which are most often located near poor and minority communities, because the Trust Fund will have be drained for other priorities. They will realize that by emphasizing liability allocation procedures, "orphan share" funding at sites with viable PRPs, and devoting all the new taxes to reducing current PRP liability, lawmakers have placed a higher priority on reducing PRP costs than on site cleanup.

A closer review of the bill reveals many areas where citizens lose, specifically:

- It does not fundamentally change the disastrous process that has failed to clean up sites for the last fourteen years.
- Rather than a new focus on public health, it leaves battles between EPA and PRPs (and among PRPs) over money as the dominant issue at most sites. Almost every one of the changes proposed to reduce these battles has been within EPA's discretion since 1986.
- It leaves in place the current incentives for PRPs to fight remedy selection decisions, and to delay cleanup. It only focuses on cost allocation.
- While reducing the liability of huge PRPs by hundreds of millions of dollars per year, it provides not one dime of increased funding for cleanup, especially at orphan sites.
- It promises more citizen participation in the process, and resources to make that effective, but doesn't provide new financing. And it doesn't remove the reasons why EPA and PRPs resist community involvement today: the money battles.
- It calls for more and faster public health assessments, with more community input, but again provides no new financing.
- If its new promises are all funded, it could reduce current cleanup spending from the Trust Fund by over $500 million per year, because it provides no new financing sources for these new promises.
- It has rhetoric about community development, but has no training programs, no contracting opportunities, no focus of existing programs on harmed communities, and no liability change to stop the incentive to avoid "brownfields."

Environmental justice concerns cannot be addressed by a section heading at the back of a bill. Our concerns are not "add-on" items. The central environmental justice concern is how the central purpose of Superfund -- clean up -- is carried out. This requires fundamental reform.

I feel absolutely certain in saying today that if you enact this bill, which fundamentally maintains the current law with the current financing system, you will come back here in a few years, long after the congratulations and smiles at the bill signing, explaining to citizens, but probably not very persuasively, what went wrong. In other words, you may be able to pass a bill which does not fundamentally reform Superfund, but, if you do, you most assuredly will not solve the problem.

We say it's time to make fundamental change in Superfund. And change -- and boldness -- is what ASAP's Eight Point Plan is all about.

Very clearly, citizens do not win under this bill. As it now stands, the Administration bill includes promises for more public participation, site reprioritization, public health initiatives and environmental justice, but they are empty promises for two simple reasons -- no new funding accompanies them, and the dynamics which prevent them have not been changed. When new programs are authorized but not newly funded, money must be taken from some other program. This means that if these initiatives were funded, cleanup spending would likely decrease. And that is directly counter to the goal of more and better cleanup.

As the proverbial checkwriters of this very important program, I encourage you to fully study S. 1834 and truly understand where the financing is coming from, where it is going to, and who really benefits from the inside deals. If you look at the attached chart, you will see that the financing priorities of S. 1834 are exactly backwards.

Financing Priorities

Let me describe the chart, working from left to right. First, the Superfund program spends about $1.5 billion per year. The rest of the chart shows increases and decreases from that base.

The key to understanding this chart is knowing what EPA does with the Trust Fund today. About $900 million to $1 billion of the total is spent on cleanup related work today. The rest is spent on lawyers and enforcement, research, and overhead. $200 million of the cleanup money is spent for emergency removals. The balance of $700-800 million is the only source of cleanup money for orphan sites, which tend to be located in poor and minority communities.

Cleanup is not happening in these communities because of shortages of funds in the Trust Fund -- those this cleanup account should be increased. But the opposite is done under S. 1834.

EIRF

You are being asked to vote new taxes of $500 million per year, rising rapidly to over $1 billion to fund a huge new business entitlement program. The Environmental Insurance Resolution Fund (EIRF) is the only new program in the entire Administration bill to be financed from new taxes. However, ironically, the EIRF provides no additional money for public health and cleanup programs. It has nothing to do with cleanup -- indeed EIRF money gets paid out to PRPs even if they are fighting the Government at every site. The

hundreds of millions of dollars in new taxes (on insurers) will be used only to reduce the existing liability and past expenses of solvent PRPs. Worse, the new tax revenue will pay for past PRP costs, including PRP legal fees dating back to 1981.

Orphan Share Fund

The bill sets aside $300 million directly from the $1.5 billion cleanup fund -- not new sources -- for an orphan share fund. This fund finances the shares of identified parties who are insolvent or defunct plus MSW generator and transporter shares that exceed the 10 percent cap, and the excess shares of parties with an inability to pay. The Orphan Share Fund is not directed at orphan sites -- the sites without PRPs where Trust Fund money is needed the most. It simply reduces the liability of the big companies which EPA pursues today.

But there are no new financing sources in the bill to pay for this.

From the beginning of the idea of a special orphan fund, which was proposed by the National Commission of Superfund last fall, every proponent swore that it would be funded by "new money" and would not reduce the current Trust Fund's resources. Quite obviously this is not happening. Indeed, in anticipation of the passage of S. 1834, the Senate Appropriations bill just cut the discretionary part of the Superfund Trust Fund from $1.5 billion to $1.2 billion.

Again, valuable cleanup dollars are being spent on reducing the liability of solvent PRPs, rather than being spent to improve the health of many communities. Clearly, the Administration is putting saving businesses money ahead of cleanup.

Increased Government Transaction Costs

Due to the series of additional burdens the new liability allocation process places on the Government, we estimate the Government's own transaction costs will increase by approximately $50 million. This will have to come out of the current, fixed pot of the Trust Fund, just like the Orphan Share Fund.

Unfunded Promises

As mentioned above, the Administration bill attempts to add citizen acceptance to the bill by promising various citizen and public health programs. The bill proposes unfunded programs with a total price tag of $160 million more for community and health needs ($13 million for ATSDR, $40 million to subsidize PRPs' use of innovative technologies if they fail, $50 million for Citizen Information and Access Offices and $60 million for technical assistance grants to community groups). Among the additional unfunded promises/programs are community working groups support; increased research, development and training demonstration grants, and assistance to state voluntary cleanup programs.

However, no new financing is provided for any of these programs. If the government should follow through with its promises and provide financing for the various programs, that can only come out of current Trust Fund spending on cleanup. The Senate just added another unfunded promise to buy the support of a citizen's group: authorization to spend the Superfund on primary health care clinics at sites.

I know some citizen leaders are supporting HR 3800 because they were promised new programs. The bill's supporters ought to be honest with them about the absence of new financing.

Impact on Trust Fund Cleanup Spending (assuming promises are not funded)

The orphan share fund is mandatory; it has a first claim. EPA and DOJ transaction costs will have to go up or the whole system of S. 1834 will collapse. Only counting these changes, the Trust Fund money available for cleanup will be reduced by $350 million annually -- or thirty five percent.

Impact on Trust Fund Cleanup Spending (assuming promises are funded)

If the rest of the new promises are fully funded, the Trust Fund money available for cleanup will be reduced by over $500 million annually -- half.

This is an outrage.

A Better Alternative -- the Eight Point Plan

I encourage you to consider carefully the lack of funding in this bill. If you simply rubberstamp this bill, you will simply be approving a tax hike on insurers -- a tax which finances a fund that is not even spent on cleanup, while reducing cleanup funds.

Instead, I encourage the Committee to look to alternative mechanisms where these additional monies can be used directly to improve the health and well-being of hundreds of communities across the country.

It will increase the number, speed and efficiency of cleanups, protect public health and the environment, reduces wasteful conflict and transaction costs, provide for greater public participation and community empowerment, and promote economic redevelopment. These initiatives and programs are financed through increased taxes on business, replacing the failed site-by-site retroactive liability system. Our bill substantially increases spending on cleanup, and provides the funding for new initiatives.

On behalf of ASAP, I urgently request that you review our bill, and that you vote to

create new taxes and new fees, but condition your funding increases on the program being fundamentally reformed along the lines of the ASAP comprehensive reform bill.

Why Businesses Support Increased Business Taxes to Fund Superfund

The business members of the Alliance for a Superfund Action Partnership (ASAP) and thousands of other businesses across the country support increased broad-based business taxes in exchange for the elimination of retroactive, site-specific Superfund liability.

Early this year the Business Roundtable formally voted to support up to a doubling of the Environmental Income Tax "if necessary" to support liability reform. (Some of its members now strongly support the Administration bill because it gives them huge liability reductions without paying any increased taxes!)

The reasons why so many businesses support higher taxes in exchange for reforming retroactive liability are straightforward:

- Business today spends around $4 billion a year on NPL Superfund sites, but cleanup spending generally is about at $2.3 to 2.5 billion. Over $1 billion a year is wasted on lawyers, litigation quality testing and other non-cleanup activities because of Superfund's retroactive liability system.

- Augmenting the $4 billion spent by business are the economic consequences of the uncertainty created by the Superfund liability system and the length of time it takes to resolve how much each PRP owes.

- Some very large PRPs can absorb the uncertainty caused by contingent Superfund liability, but most of the 32,000 PRPs now tangled in the process find it difficult. For most, the uncertainty impedes investment and management decisions and impairs access to capital.

- The U.S. Small Business Administration earlier this year said that "any meaningful reform of the liability scheme must include elimination of retroactive liability for waste disposal prior to January 1, 1987. Small businesses generally were not required to maintain records of waste disposal prior to that date. Otherwise, small businesses are placed in the inequitable position of defending their actions without records."

- The number of businesses affected will swell as more sites proceed into the PRP identification phase and new sites are brought into the system. A tax-based financing system will establish a rational, well defined and well understood funding scheme for the Superfund program, as well as a finite budget.

- In the aggregate, businesses support a tax-based approach because it would be far

more efficient than the current site-by-site financing battles. It would cost the business community no more than it currently is paying (and probably less), and more would be spent on cleanup and the other important priorities ASAP has.

There is no secret to this widespread business support for liability reform. The current system hurts them. They therefore are offering more money to address the cleanup concerns of affected communities if they can be relieved of the uncertainty and huge legal fees that the present system imposes on them. It seems to me inconceivable that Congress would not respond to taxpayers who are asking to be taxed and to a plan that promises more and faster cleanup of our communities.

it is for these reasons that conservative Republicans like Senator Bob Smith and Rep. Bill Zeliff have introduced legislation doubling the EIT and raising insurance taxes to replace retroactive liability.

Conclusion

The failures of Superfund are well documented: the unconscionably inadequate cleanup record, the staggering waste of public and private resources on legal and liability battles, the disenfranchisement of citizens which erodes confidence in government at all levels, and the suppression of economic dreams as entire communities wait, and wait, and wait for action.

Let us not settle for reform which falls well short of addressing these problems. Enactment of a bill is not what should drive us. Instead, we should only settle for a bill that truly gets the job done. We would prefer no bill at all to one which perpetuates in the name of reform many of the injustices and failures in place today.

Let us not mistake cobbling together a bill which satisfies some vocal and visible constituencies for a bill which will result in a successful program. Such a bill may be politically feasible, but if it doesn't work, it's not much help to anyone.

Thank you. The members of ASAP and I look forward to working with you.

COMMUNICATIONS

STATEMENT OF THE ALLIANCE OF AMERICAN INSURERS

The Alliance of American Insurers is a national trade association of 215 property/casualty insurance companies, writing insurance in all 50 states and the District of Columbia.

The Alliance and its members support the goal of quick and effective cleanup of hazardous waste sites. There are many provisions in S. 1834 that promote this goal. Unfortunately, Title VIII and its funding mechanism, Subtitle A of Title IX, are not among them. Because we believe that the Environmental Insurance Resolution Fund (EIRF) created by Title VIII of this bill is fundamentally flawed and that there is no way to fund it that is equitable to all segments of the property/casualty industry, we urge this committee to strike Subtitle A of Title IX from S. 1834. Superfund reform should move forward this year. However, it should move forward without Subtitle A of Title IX and without Title VIII.

THERE IS NO WAY TO FUND THE EIRF THAT IS EQUITABLE, OR WILL PRODUCE CONSENSUS AMONG INSURERS

There are several problems that are presented by any funding mechanism for the EIRF.

A. It is unfair to all insurers and their customers

Any taxing scheme for the EIRF will raise $8.1 billion over 10 years from property/casualty insurers. Thus insurers, assuming the best possible case, will pay $8.1 billion to replace liabilities that they never intended to write and for which they collected no premium. These taxes will be paid by innocent insurers and their even-more-innocent customers in today's insurance market.

B. The property/casualty industry is irreparably split

There is no consensus among property/casualty insurers in support of any funding mechanism. The current House Ways and Means proposal is supported only by one trade association and one company, and has received no support from the other 65 percent of the insurance industry. Neither 100 percent prospective nor 100 percent retroactive taxes are supported by a majority of the industry, and neither was the 70 percent retrospective/30 percent prospective split originally in H.R. 3800.

Companies that never wrote commercial liability business believe it is unfair for them to pay for liabilities imposed on those who did. Companies that wrote commercial liability believe they will be at an unfair competitive disadvantage unless any tax is prospective and can be added on as an equal additional cost of doing business industry-wide. There is no middle ground between these two positions on which a majority of the industry can reasonably accept this new tax (for which insurers get nothing in return).

C. Any funding method for the EIRF as currently structured is a misguided attempt to redistribute Superfund liabilities solely within the insurance industry

A central belief of the Alliance is that all of society shared in the benefits of the activities that produced the hazardous waste which Superfund is designed to clean up. Therefore, we believe that all of society should share in the costs of that cleanup. As property/casualty insurers, we are willing to bear an appropriate share of that burden. However, we believe that the rest of society should share the burden as well. That is why we support a trust fund whose funding is spread across our entire society as the mechanism to clean up Superfund sites.

All of the proposed funding mechanisms for the EIRF, however, simply reallocate insurers' potential Superfund liabilities solely within the property/casualty insurance industry. Since this is the case, it is easy to understand why no funding mech-

anism commands consensus support from the industry. Both the base of the taxation and the distribution are too narrow.

D. Increasing the taxes on commercial insurers will invariably lead to an acceleration in self-insurance

As the EIRF tax is implemented and increased, it would be added to premium taxes and other "involuntary market" taxes already paid by insurers. This would erode traditional insurers ability to compete with self-insurance arrangements and other types of lesser-regulated risk management mechanisms. This would be a recipe for additional problems for both insurers and policyholders down the road.

E. The amount of the fund is wholly inadequate

Even if the EIRF becomes fully operational, it still would not provide a comprehensive solution for the potential universe of environmental liability claims that exist between insurers and their policyholders. The EIRF only applies to federal sites appearing on the National Priority List (NPL). Currently, there are over 1,200 sites on the NPL. However, EPA has calculated that some 36,000 sites require remediation. In other words, EIRF would not cover approximately 97 percent of federal sites—nor would it cover any state sites. Litigation at those sites would continue unabated.

If the EIRF were expanded to cover all potential NPL sites, or other non-NPL sites, both the amount of the fund ($8.1 billion) and the base of the fund would have to be significantly expanded. Yet either of these scenarios would be problematic for EIRF. Insurance company rating agency A.M. Best Co. recently estimated that total property/casualty insurance industry exposure to environmental liabilities is well over $200 billion. Yet total insurance industry surplus as of December 31, 1993, stood at $183 billion. Clearly, a larger EIRF would require a broader base than just the insurance industry.

THE ENVIRONMENTAL INSURANCE RESOLUTION FUND WILL NOT ACHIEVE THE PUBLIC POLICY GOALS OF SUPERFUND REFORM

The EIRF does not address the fundamental causes for the delay in cleanup of Superfund sites, and therefore, cannot work to speed cleanup of sites and/or substantially reduce transaction costs. The real causes of the program's failures to date are: (1) the retroactive, strict, joint and several liability regime in the current Superfund law; and, (2) the courts' refusal to honor clearly-drafted insurance policy exclusions.

Retroactive liability imposes liability without notice upon persons who were acting legally when they committed the acts that subject them to Superfund's remedial provisions. Strict and joint and several liability allow parties who caused little, if any, of the damage to be liable for the entire cost of cleanup. And the fact that many courts have refused to properly interpret clear insurance policy language excluding coverage from all but "sudden and accidental" pollution has spread the costs of Superfund to insurers that did not intend to insure against environmental damage and collected no premiums to do so.

The result of this is the massive and protracted litigation we see today, as potentially responsible parties (PRPs) and the Environmental Protection Agency cast about for anyone they can sue and insurers try to defend the pollution exclusions in the policies they wrote. With the current liability structure, it is no wonder that so few sites have been cleaned up. Elimination of retroactive, strict, joint and several liability and institution of a broad-based trust fund would eliminate much of the litigation and make it much more likely that hazardous waste sites will be cleaned up efficiently and expeditiously.

Unfortunately, the EIRF does not bring us closer to any of these goals. Rather, it is an attempt by *a few* insurers in the property/casualty industry to apply a mere palliative, a Band-Aid applied to a hemorrhaging artery. This "solution" will do little to cure the ills of Superfund, but temporarily may make it seem as if the pain has gone away. True Superfund reform must deal with the root causes of the current system's problems, and the EIRF sidesteps those problems.

EIRF WILL INCREASE THE BURDEN OF SUPERFUND LIABILITY ON INSURERS

There is a fundamental adverse incentive in the EIRF's structure that makes it possible that the EIRF will *increase* the amount of money that insurers are required to pay under Superfund. This is caused by the EIRF's 60 percent/40 percent/20 percent settlement structure.

The 20 percent states are those whose courts have generally upheld the pollution exclusion in 1970s-vintage commercial general liability policies. PRPs that would be required to bring suit in those states have a strong incentive to accept the EIRF's

offer and receive 20 percent of their costs from the EIRF, rather than risking losing their coverage lawsuits and receiving nothing. The 60 percent states are those in which courts have generally held in favor of PRPs in their coverage litigation. PRPs in those states have an incentive to continue their litigation because they may have a substantial chance to recover 100% of their costs, rather than the 60 percent maximum EIRF offer. Thus insurers may get little or no benefit from the EIRF with respect to PRPs in the most unfavorable states, while having to pay 20 percent to PRPs in states where they might well pay nothing otherwise.

At the same time, PRPs in 20 percent states will be pressing Congress to make their state a 40 percent state; those in 40 percent states will seek to become 60 percent states. This exercise in rough justice is political nonsense.

IT WILL BE EASIER TO PASS A SUPERFUND BILL IF THE EIRF IS REMOVED

The only point on which a great majority of the property/casualty insurance industry could agree is that the EIRF is fatally flawed and should be removed from this bill. If it is removed, the property/casualty industry is likely to either support or remain neutral with respect to the rest of H.R. 3800/4916. The Alliance of American Insurers would support S. 1834 if Title VIII and Subtitle A of Title IX were removed. To the extent that the discord within this industry has jeopardized the passage of Superfund reform this year, that obstacle will be removed.

CONCLUSION

The Alliance of American Insurers respectfully urges the Senate Finance Committee to strike Subtitle A of Title IX from S. 1834. We also would urge that Title VIII of S. 1834 be struck from the bill when it reaches the Senate floor.

STATEMENT OF THE AMERICAN PETROLEUM INSTITUTE

This statement is submitted on behalf of the American Petroleum Institute (API) for the record of the Committee on Finance, September 14, 1994 hearing on the financing provisions of the Administration's Superfund proposal, S. 1834, the Superfund Reform Act of 1994.

API represents approximately 300 member companies involved in the exploration for and production, refining, transportation, and marketing of petroleum and petroleum products. API members will be significantly affected by the changes that Congress elects to make to the Superfund program—as members of the community, as potentially responsible parties (PRPs), and as taxpayers. Much about Superfund needs to be changed, and Administration officials and members of Congress are to be commended for their efforts to remedy the current law and regulations.

THE CURRENT SUPERFUND TAX SCHEME

A major area that needs reform is the current inequitable CERCLA funding scheme which imposes the majority of the taxes on one industry and its products. The Superfund program is intended to clean up "orphan wastes" disposed of in the past by companies which no longer exist, are not solvent or cannot be identified. Identified, solvent parties must themselves clean up or pay for the cleanup of any wastes for which they are responsible. Furthermore, the evidence is incontrovertible that responsible parties for abandoned hazardous wastes that have accumulated over many years encompass a wide range of companies, industries and government agencies of all sizes and types located throughout the United States. The need to pay for the cleanup of the "orphan wastes" is a broad societal problem that should be paid for through general revenues or broadly based funding sources. Recognizing these concerns, Congress included the broad-based Corporate Environmental Tax as one source of funding when it reauthorized CERCLA in 1986.

Yet, despite that action, the petroleum industry continues to pay between 55 and 60 percent of the taxes dedicated to financing Superfund. The API supports an extension of the Superfund of the size the Administration has proposed. However, we continue to believe that more of the funding should be provided through general revenues or broad-based taxes. Three tax sources, in addition to modest general revenues, provide dedicated funds for the Superfund Trust Fund. Petroleum companies make payments to the federal government under each of these taxes: the tax on petroleum, the tax on chemicals, and the corporate environmental tax. Data on each of these taxes, and the petroleum industry's share, are summarized below and in the attached table.

Tax on Petroleum:

According to Internal Revenue Service reports on excise tax collections, the petroleum tax generated $547.6 million in 1988, $570.5 million in 1989, and $545.2 million in 1990 (calendar year data). This amount is paid only by companies operating in the petroleum industry.

Tax on Chemicals:

According to the same Internal Revenue Service reports, $294.3 million was collected under the chemical tax in calendar year 1988. For 1989 and 199C, $277.7 million and $296.0 million were collected, respectively. According to estimates based on plant level chemical production capacity as reported by the Chemical Economic Handbook, the share of the chemical tax paid by petroleum industry companies is in the 56 percent to 63 percent range.

Using the 56 percent to 63 percent range as the petroleum industry's share of the chemical tax yields petroleum industry chemical taxes of $152 million to $189 million per year over the 1988 to 1990 period, as shown in the attached table.

Corporate Environmental Tax:

The U.S. Department of the Treasury reports that $487.9 million, $471.8 million, and $520.2 million in corporate environmental taxes were collected in calendar years 1988, 1989; and 1990, respectively.

The petroleum industry's share shown in the attached table—8.6 percent for 1988 and 9.4 percent for 1989, and 11.6 percent for 1990—is the total for two industry categories contained in the Treasury data. These are "oil and gas extraction" and "petroleum (including integrated) and coal products." Based on the Treasury data, the petroleum industry paid $42.0 million, $44.5 million, and $60.4 million in corporate environmental taxes in 1988, 1989, and 1990, respectively. Totals for Petroleum, Chemical, and Corporate Environmental Taxes:

Based on the above data, it is estimated that during 1988, 1989, and 1990, the petroleum industry paid about 57 percent to 60 percent of the total petroleum, chemical, and corporate environmental taxes dedicated to financing the Superfund Trust Fund.

Petroleum Industry's Contribution to NPL Site Contamination:

Very limited data are available on a given industry's likely share of contamination at Superfund sites on the current national priorities list (NPL). An Environmental Protection Agency report, Superfund NPL Characterization Project: National Results, includes survey information on "industries responsible for generating the wastes that occur at the site." The report indicates that about 52 percent of the sites have wastes generated by the manufacturing industry. At the sites with manufacturing industry generated waste, 8.5 percent of the sites have wastes from "petroleum refining and related industries." Based on the EPA Superfund NPL Characterization Project: National Results report, about 4.4 percent (8.5 percent times 52.2 percent) of NPL sites have wastes generated by "petroleum refining and related industries."

It has been observed that the petroleum industry also owns some mining facilities and chemical plants. It is unclear from the EPA report whether the "related industries" in the "petroleum refining and related industries" category includes the mining or chemical facilities owned by petroleum companies. However, even doubling the 4.4 percent figure, to allow for the possibility that some wastes from petroleum industry owned mining and chemical operations are reported in other categories, implies that the petroleum industry may be a major contributor of wastes at less than 10 percent of the NPL sites.

Although the petroleum industry pays almost 60 percent of the Superfund taxes, it is responsible for only a very small portion—less than 10 percent—of NPL site contamination problems.

Given this clearly inequitable imposition of the tax burden, API strongly believes that the CERCLA tax base should be broadened.

DIVERSION OF THE CORPORATE ENVIRONMENTAL TAX

The Section 59A Corporate Environmental Tax (CET), enacted as part of the 1986 Superfund Amendments and Reauthorization Act (SARA), is one of the taxes dedicated to the Superfund Trust Fund. IRC Section 9507 provides that amounts equivalent to the taxes received in the Treasury under Sections 59A, 4611, 4661, or 4671 are appropriated to the Superfund, and that amounts in the Superfund shall be available only to make expenditures to carry out specified purposes of CERCLA. API opposes recent proposals to divert revenues generated by the CET to other purposes.

The Superfund taxes are due to expire December 31, 1995. S. 1834 provides that these taxes be reauthorized at their current rates through December 31, 2000.

The Administration has proposed—as a part of S. 1834's reform of the CERCLA liability provisions—to create a new mandatory "orphan share" spending program, scored as funded by revenues from the reauthorized CET. This provision is a crucial part of the move to proportional liability—the basic reform of the CERCLA liability system contained in the Administration's bill. It was API's understanding that, under the Administration's proposal, the cost of orphan share cleanup would be adequately funded without any additional taxes. Because the budget baseline does not include an assumption that the CET will be reauthorized, revenues from the reauthorization of the CET may be scored against mandatory spending programs; hence, under S. 1834 no new taxes would be needed to fund the orphan share program.

Unfortunately, the Administration has recently proposed scoring revenues from reauthorizing the CET to partially fund other programs, including welfare reform and the GATT implementing legislation. (They have subsequently withdrawn the GATT funding proposal, but continue to propose the CET as an offset for welfare reform.)

The Office of Management and Budget (OMB) contends that there is sufficient revenue from CET reauthorization to score for both purposes—Superfund orphan share funding and welfare reform. Furthermore, regarding their proposals to budget score CET for purposes other than Superfund, the OMB insists that "no Superfund receipts will be used for anything other than the Superfund program" and that the appearance that Superfund taxes are being used to fund some other program is "simply the result of budget scorekeeping conventions." Nevertheless, we are concerned that because the Congressional Budget Office estimates for CET reauthorization are significantly lower than OMB's estimates, there is not sufficient revenue to offset both the Superfund orphan share program and welfare reform.

Furthermore, even the appearance of diverting revenues from the Corporate Environmental Tax to purposes other than that for which it was enacted raises the specter that it can be severed from its environmental purpose which would break faith with those industry groups that were party to the 1986 SARA agreement and could cause some to oppose its reauthorization.

We urge the Committee to reject any proposals to use revenues from the Corporate Environmental Tax for other than its statutorily mandated purpose.

ENVIRONMENTAL INSURANCE RESOLUTION FUND

S. 1834 establishes a new Environmental Insurance Resolution Fund (EIRF) intended to eliminate disputes over liability coverage for cleanup costs between insurance companies and their insureds who are potentially responsible parties (PRPs). The EIRF would provide settlement of insurance claims related to Superfund liability for pre-1986 disposal of waste. The Environmental Protection Agency estimates that litigation over these claims costs approximately $300 million per year.

The EIRF is financed under the bill by two types of "fees" on applicable casualty insurance policies: the first imposed on insurance premiums written during the 15 calendar year period beginning with calendar year 1971 (the retrospective fee), and the second imposed on premiums on policies written after date of enactment of the bill (the prospective fee). According to the Administration, the bill is intended to impose 70% of the cost of the EIRF on the retrospective fee and 30% on the prospective fee.

As policyholders and PRPs, and as payers of the lion's share of the current Superfund taxes, API's members are concerned that they not be additionally burdened by these new fees which are designed to relieve insurance companies of liability coverage for pre-1986 actions.

Estimated Superfund Taxes Paid By Petroleum Companies
(Million Dollars)

	1988	1989	1990
Petroleum Tax:			
Total collected [1]	$547.6	$570.5	$545.2
Petroleum industry:			
Estimated share	100%	100%	100%
Estimated total	$547.6	$570.5	$545.2
Chemical Tax:			
Total collected [1]	$294.3	$277.7	$296.0
Petroleum industry:			
Estimated share [2]	58% - 64%	55% - 62%	56% - 62%
Estimated total	$170.4 - $188.9	$151.6 - $170.8	$164.3 - $183.2
Corporate Environmental Tax:			
Total collected [3]	$487.9	$471.8	$520.2
Petroleum industry:			
Estimated share [3]	8.6%	9.4%	11.6%
Estimated total	$42.0	$44.5	$60.4
Total of Above			
Total collected	$1,329.8	$1,320.0	$1,361.4
Petroleum industry			
: Estimated share	57% - 58%	58% - 60%	57% - 58%
Estimated total	$760.0 - $778.5	$766.6 - $785.8	$769.9 - $788.8

[1] As reported in Internal Revenue Service "SOI Bulletin" for Winter 1992-93; Winter 1991-1992 (Volume 11, Number 3); and Fall 1990 (Volume 10, Number 2), calendar year data.

[2] See API paper, "Revised Estimates of Superfund Chemical Taxes Paid by Petroleum Companies" (6/30/94), for details of this estimate. Briefly, the estimates are based on individual plant capacity data for 5 petrochemicals. These 5 petrochemicals (benzene, ethylene, propylene, toluene, and xylene) accounted for about 90 percent of petrochemical tax revenue and 71 percent of all chemical taxes in 1990, and similar shares in 1988 and 1989. The lower estimate excludes any taxes paid on 6 other taxed petrochemicals for which capacity data was not obtained. The higher estimate assumes the petroleum industry capacity tax shares for these 6 petrochemicals was the same as the average of the 5 petrochemicals for which data was obtained.

[3] U.S. Department of the Treasury, "1988 Statistics of Income: Corporate Income Tax Returns," Publication 16 (Rev. 11-91), Tables 1 and 2; "1989 Statistics of Income: Corporate Income Tax Returns", Tables 1 and 2; and "1990 Statistics of Income: Corporate Income Tax Returns", Tables 1 and 7. Petroleum industry share is the sum of "Oil and gas extraction" and "Petroleum (including integrated) and coal products" categories.

STATEMENT OF THE ASSOCIATION OF FINANCIAL GUARANTY INSURORS

The Association of Financial Guaranty Insurors ("AFGI") appreciates the opportunity to submit its views on the financing portion of the "Superfund Reform Act of 1994." AFGI is comprised of nine "AAA" rated U.S. companies whose sole business is guaranteeing the debt service of bonds issued by state and local governments, as well as mortgage backed bonds and asset backed bonds.

AFGI is submitting this statement because of its deep concern with a provision that would impose a tax on financial guaranty insurance premiums, which was included in H.R. 3800 as passed by the House Ways and Means Committee.

Because financial guarantors have never been involved in providing pollution liability insurance and, in fact, are prohibited by law from offering such insurance, a tax such as that proposed by the House Ways and Means Committee would do serious harm to state and local governments that depend on these companies to reduce the cost of raising capital for various public purpose projects such as building and maintaining the infrastructure.

In testimony by Assistant Secretary Leslie Samuels before the Senate Finance Committee on Wednesday, September 14, the Treasury Department proposed that financial guaranty insurance be exempted from the lines of insurance subject to the new tax. AFGI strongly supports Treasury's proposal to exempt financial guaranty insurance, and is submitting this statement in order to assist the members of the Finance Committee in understanding the nature of financial guaranty insurance, its extremely important role in municipal finance, and the reasons why a Comprehensive Environmental Response, Compensation, and Liability Act of 1980 ("CERCLA") or Environmental Insurance Resolution Fund ("EIRF") tax on this line of insurance would be inappropriate.

THE FINANCIAL GUARANTY INSURANCE INDUSTRY

Financial guarantors are like no other type of insurance company. In fact, our competition in the market for credit enhancing bonds is the bank letter of credit. Thus, while it is true that financial guaranty insurers are regulated by state insurance laws, the business of these companies is unlike that of any other type of insurer.

Although financial guaranty insurers provide insurance for bonds issued for such purposes as building bridges, hospitals and airports, these companies do not insure the underlying structures for which the bond proceeds are to be used. It is up to the municipal issuer that is financing construction of the bridge, for example, to obtain any necessary insurance, such as liability and fire coverage, on the structure itself.

By law, financial guaranty insurers are prohibited from writing other lines of insurance that are unrelated to financial guaranty insurance. A company that is chartered as a financial guaranty insurer is, therefore, required to be monoline.

The reason for this requirement is that insurance regulators have recognized that guarantors of bonds, although experts in the analysis and judgment of creditworthiness, take on significant amounts of risk. In calendar year 1993, financial guaranty insurers guaranteed municipal bonds having a par value of over $108 billion.

Because approximately 50 percent of municipal bonds finance the development or maintenance of state and local infrastructure and because the overwhelming majority of municipal debt is owned by individuals, these companies serve a vital role in providing safety and liquidity for the capital markets. It was, therefore, determined that financial guaranty insurers should not take on other types of risk that could adversely impact their ability to make good on their promise to make timely payments of principal and interest when due on any insured bond.

It is worth noting that these companies are regulated by more stringent standards than any other type of insurance company. For example, financial guaranty insurers are required to have and maintain approximately 15 times as much capital as any other type of insurer.

Moreover, other than mortgage guaranty insurers, which the Ways and Means Committee exempted from the proposed tax, only financial guaranty insurers are required to maintain contingency reserves in addition to the reserves maintained for losses and the expenses related to such losses. Contingency reserves are established to protect against a depression type scenario wherein many state and local governments become bankrupt, thereby requiring financial guarantors to cover principal and interest payments on all insured bonds.

However, it is not only the most stringent insurance laws that set financial guaranty companies apart from all other types of insurers. In order to operate as a financial guaranty insurer, the market for credit enhanced bonds demands that the

insurer be rated "AAA" by at least one, and preferably more than one, major credit rating agency such as Moody's or Standard & Poor's.

Once a financial guaranty company receives a "AAA" rating, the rating agency reviews each risk insured to make certain that the risk is at least investment grade on an uninsured basis and that the insurer's capital can support the new exposure. Although it has never happened, a company downgraded below a "AAA" would be unable to function as a financial guaranty insurer.

In addition, traditional insurance companies operate with the expectation that a certain percentage of the insured risks covered will actually suffer losses, requiring a loss payment to the insured. Financial guaranty insurers, by contrast, underwrite to a "zero loss" standard—that is, with the expectation that the covered risk—default—will not occur. It should also be noted that financial guaranty insurance does not make payments to the insured in case of default, but rather to the bondholder investor. Because the insured would not receive any payment from the financial guaranty insurer, such insurers do not have even indirect liability for any potential pollution problem.

Furthermore, unlike property and casualty insurers, which are subject to guaranty fund assessments in all states they write business, financial guaranty insurers are exempt from guaranty fund assessments in over 45 states. In fact, the financial guaranty insurance line is exempt from guaranty fund assessments in all states. However, in a few of the states that have not enacted financial guaranty insurance laws and that consider such insurance a form of surety insurance, financial guaranty insurers are subject to assessments because the surety line is subject to assessment.

THE IMPORTANCE OF BOND INSURANCE

Bond insurance is important to the stability, safety, cost-effectiveness, and efficiency of the municipal bond market. First, using insurance can significantly reduce issuers' costs of financing by enabling them to sell bonds at a lower interest rate. Investors seek safety by buying insured bonds even at the cost of receiving a lower return. This has become increasingly important as the profile of bond investors has changed over the past decade from one dominated by institutional investors to one today where approximately 64% of all outstanding municipal debt is owned by individuals either directly or through mutual funds or unit investment trusts.

Bond insurance increases the speed at which issuers can come to market, and insurance improves the marketability of bonds. Insurance helps bonds to retain their value even if the rating of the issuer is downgraded, compared to the uninsured bonds of the same issuer. Insured bonds are generally more liquid because the insured bonds retain the triple-A rating of the financial guarantor even if the issuer's rating is downgraded.

Because of these benefits, the insured portion of the municipal bond market has been steadily growing. Last year around 40% of new issuance was insured.

FINANCIAL GUARANTORS SHOULD NOT BE SUBJECT TO THE SUPERFUND TAX

As citizens of various communities affected by hazardous waste sites, AFGI members support any measure that will help in the cleanup efforts by resolving disputes between responsible parties and their insurers over the costs of such cleanup. However, because financial guarantors have never been involved in any way with the provision of environmental liability insurance, a tax on the future premiums written by these companies to help fund the EIRF would bear no relationship to the type of risks covered by these companies.

Moreover, because financial guaranty insurers have never collected and will not in the future collect any premiums related to the types of insurance implicated in the CERCLA, the essence of such a proposal would be to tax the capital of such companies. A tax on the capital of such a capital intensive industry could have serious adverse consequences for the future capacity of financial guarantors.

As a result of individuals investing in ever increasing amounts of municipal bonds, state and local governments have increasingly sought the "AAA" rating that comes with the guaranty provided by financial guarantors on insured bond offerings. Thus, the growth in the par value of municipal bonds insured has increased from $38 billion in 1990, $59 billion in 1991, over $85 billion in 1992 and more than $108 billion in 1993.

In addition to having adverse consequences on the ability of financial guaranty insurers to provide the necessary capacity in the future, the proposed tax imposed by H.R. 3800 would have serious implications for various state and local governments. Insurers will attempt to pass at least a portion of the new tax on to their customers, the state and local governments that purchase such insurance. The bur-

den of paying this tax will make it more costly for municipal governments to raise money and, in some instances, may discourage some governments from going forward with bond offerings intended to raise funds for the building or maintenance of infrastructure.

Finally, while some of the other lines of insurance included in the prospective tax are not related to pollution liability claims, in many instances such lines of insurance are sold by multi-line insurance companies which—as a company—do receive a benefit from the EIRF program. By contrast, because financial guaranty companies are monoline, they will not receive any benefit from the EIRF fund—and yet they are still being taxed for this program as if they will receive a benefit.

CONCLUSION

Although H.R. 3800 recognized that certain lines of insurance have no relationship to environmental liability insurance and so were exempted from the imposition of the new tax, the House Ways and Means Committee proposed taxing financial guaranty insurers, which by law are prohibited from providing such insurance. Because of the very serious adverse consequences to the financial guaranty insurance industry as well as to state and local governments who depend on financial guarantors to raise funds at reduced costs, the members of AFGI urge this Committee to exempt financial guaranty insurance from any CERCLA or EIRF tax imposed on segments of the insurance industry.

STATEMENT OF JAMES BALLER

Dear Chairman: We appreciate this opportunity to respond to the Senate Finance Committee's solicitation of public comments on the revenue and other aspects of S. 1834, the "Superfund Reform Act of 1994."

We focus our comments on the portion of S. 1834 that would transfer to the Environmental Protection Agency (EPA) the authority that the Agency for Toxic Substances and Disease Registry (ATSDR) now has to conduct health assessments and related activities at Superfund sites. This action was apparently intended to respond to claims by certain community activists that ATSDR has not been responsive enough to the concerns of communities living near Superfund sites.

These comments are based upon the many years of experience that Dr. George L. Carlo, Kelly Sund and I have had with public health issues and ATSDR. Dr. Carlo, in fact, was one of the principal draftsmen of the language in the Superfund Amendments and Reauthorization Act of 1986 through which Congress expanded and spelled out ATSDR's responsibilities in detail. The views expressed in these comments are our own and do not necessarily reflect those of all of our clients.

DEFICIENCIES IN THE PUBLIC-HEALTH PROVISIONS OF S. 1834

Under current law, ATSDR is responsible for conducting public health assessments, follow-up health-effects studies and related activities at all sites on the Superfund National Priorities List as well as at additional sites that ATSDR may select in response to petitions from the public. ATSDR is also responsible for establishing and maintaining toxicological databases, disseminating information about environmental health, educating the public and the medical community about environmental health issues and performing various other functions relating to environmental health. ATSDR is one of the eight constituent agencies of the Public Health Service, the entity within the Department of Health and Human Services (DHSS) that has been responsible for promoting and protecting the public health of our nation since 1798.

We fully agree that, to be effective, the agency responsible for performing health assessments must have the confidence of affected communities. We do not agree, however, that ATSDR has a substantial or widespread credibility problem with communities today or that, even if it did, transferring its responsibilities to EPA would be a sensible or appropriate response.

As we show in the enclosures, ATSDR had a slow and rocky start that caused it to fall short of the expectations of virtually all concerned—not just communities, but also Congress, EPA, industry, environmentalists and many others. In the last three years, however, ATSDR has dramatically improved its performance as an independent, scientifically-based and dispassionate guardian of environmental health. During this period, ATSDR has also taken numerous steps to encourage and facilitate community involvement in the health-assessment processes. As a result, relatively little opposition to ATSDR's recent work has emerged from affected communities. The lack of widespread opposition to ATSDR is particularly striking when

placed in context—ATSDR has now completed more than 1600 public health assessments, initiated dozens of follow-up health-effects studies, and issued some 4000 health consultations in each of the last several years.

In any event, even if legitimate grounds continued to exist for concern about ATSDR's responsiveness to affected communities, it would not be necessary for Congress to deal with these concerns by removing ATSDR from the Superfund process. Rather, Congress could simply enact specific statutory measures—such as those contained in H.R. 4916—that would spell out precisely what ATSDR must do in working with affected communities.

Most important, EPA and ATSDR have fundamentally different missions, philosophies and capabilities, and each makes essential contributions to the Superfund process. Unlike EPA, ATSDR focuses on identifying *actual* health risks to specific populations rather than *theoretical* risks determined primarily through mathematical modeling and conservative default assumptions. Also unlike EPA, ATSDR seeks to tailor remedies to the particular problem at hand and does not necessarily favor permanent or comprehensive remedies when lesser remedies would adequately protect human health. The presence of both agencies in the Superfund process thus helps to ensure that threats to human health are properly evaluated and that remedies selected are neither overprotective nor underprotective. In short, we submit that eliminating the perspective that the Public Health Service brings to the Superfund process through ATSDR would *waste of billions of dollars and significantly injure public health.*

INADEQUATE CONSIDERATION BY THE SENATE ENVIRONMENT AND PUBLIC WORKS COMMITTEE

The idea of transferring ATSDR's responsibilities to EPA was not the product of careful study, focused discussion or consensus among members of the Senate Committee on Environment and Public Works. To the contrary, it came up for the first time about a week before the committee voted, at a time when the committee was preoccupied with other major Superfund issues; it received little input from the public and only scant debate; and it was strongly opposed by several members of the committee:

> The Committee bill transfers the authority to carry out health assessments around Superfund sites from the Agency for Toxic Substances and Disease Registry to the Environmental Protection Agency. . . . We believes that it makes little sense to transfer this authority from Health and Human Services (HHS) to EPA. EPA is not an agency with the primary mission of determining health effects. Much of the data EPA now collects focuses on environmental media, rather than public health, and the bill directs EPA to increase its emphasis on the collection of health related data. It is more logical to keep this responsibility for collecting health data with HHS instead of requiring EPA to hire new health specialists to accomplish this task.

Minority Views of Senators Simpson, Smith, Faircloth and Kempthorne, S. Rep. No. 103–349 at 137. In the enclosures, we expand on these points and discuss several additional reasons for rejecting the majority's approach.

OUR RECOMMENDATIONS

Last winter, representing a broad cross-section of the environmental community, the National Commission on Superfund (NCS) found that inadequate funding and EPA control of ATSDR's budget have been major factors limiting ATSDR's ability to fulfill its mission. NCS recommended that Congress address these problems either by reformulating ATSDR or by creating a new agency within the DHSS that would have sufficient funding and *independence from EPA* to carry out ATSDR's current duties as well as several additional health-related responsibilities.

The bill that has emerged from the key committees in the House (HR 4916) and original form of S. 1834 submitted to the Senate would give effect to NCS's first recommendation by strengthening and expanding ATSDR. We support this approach and urge the Senate Finance Committee to adopt it. If the Committee ultimately concludes that a fresh start is required, we suggest that it embrace NCS's alternative recommendation and opt for creating a new agency within DHSS.

If you have any questions or would like additional information, please let me know. Also, if the Committee believes that oral testimony would be helpful, we would be glad to appear at the hearing of September 14.

Enclosures.

Analysis and Perspective

ABOLISHING ATSDR'S ROLE AT SUPERFUND SITES WOULD BE SERIOUS MISTAKE

By James Baller, Dr. George L. Carlo, and Kelly Sund *

Buried in the Senate Environment and Public Works Committee's lengthy superfund reauthorization bill (S 1834) is a little-noticed provision that would transfer to the Environmental Protection Agency the authority that the Agency for Toxic Substances and Disease Registry now has to conduct health assessments and related activities at superfund sites. The committee passed this provision with little advance notice and scant discussion, apparently in response to complaints by certain community activists that ATSDR has not been responsive enough to communities living near hazardous waste sites.

ATSDR is part of the Public Health Service, the entity within the Department of Health and Human Services that has promoted and protected public health in the United States for nearly two centuries (since 1798). For that reason alone, removing one of the Public Health Service's most important public health responsibilities today would be a drastic step that should be taken only after careful study, and only for the most clear and convincing reasons.

No such reasons exist. To the contrary, the Senate committee's approach is unwarranted in view of the dramatic improvements in ATSDR's work in the last three years. It is unnecessary because more direct and less draconian means are available to cure any remaining deficiencies in ATSDR's performance. It is inconsistent with the findings and recommendations of the National Commission on Superfund, which reflect the views of a broad cross section of the environmental community. It is at odds with the approach of strengthening and expanding ATSDR taken in the administration's bill now moving through the House (HR 4916, formerly HR 3800). Most important, it would waste billions of dollars and have serious adverse effects on public health.

ATSDR's History

Congress established ATSDR in the Comprehensive Environmental Response, Compensation, and Liability Act of 1980, as amended by the Superfund Amendments and Reauthorization Act of 1986.[1]

For a variety of reasons, however, the agency essentially lay dormant until Congress reauthorized superfund in 1986.[2]

In the debates preceding the 1986 legislation, environmental groups had called for—and industry had strongly opposed—a federal cause of action for environmental torts, an administrative compensation scheme for environmental injuries, and various procedural and substantive requirements that would make state tort remedies easier to obtain. As a compromise, Congress rejected these proposals and instead broadly expanded and specifically defined ATSDR's responsibilities in conducting health assessments and related activities at superfund sites.[3]

In doing so, Congress embraced a comprehensive public-health approach to environmental health issues rather than a narrow case-by-case approach.

Unfortunately, Congress also planted the seeds for most of the credibility problems that ATSDR may have today by giving EPA control over ATSDR's budget and requiring ATSDR to complete health assessments at nearly 1,000 of the nation's highest-priority sites within two years.

No mature and experienced agency could have fulfilled this impossible assignment, much less a woefully underfunded, understaffed, and overshadowed toddler of an agency that did not even have written rules or guidelines with which to work at the time. To meet its deadlines, ATSDR relied heavily upon data generated by EPA, and it labeled hundreds of health assessments as "draft" or "preliminary." To save time, it also worked largely behind closed doors, without the benefit of public input. Not surprisingly, ATSDR's initial wave of health assessments did not satisfy anyone—as the General Accounting Office and Rep. John D. Dingell (D-Mich) would later note.

In the past three years, however, ATSDR's performance has improved dramatically. It has become much more active and visible at superfund sites, acting either directly itself or indirectly through the state public health agencies of the 2[illegible] states with which ATSDR has cooperative agreements.[4]

Improvements At ATSDR

Among other things, ATSDR has published regulations that provide for notice and opportunity for public comment on draft public health assessments; issued a detailed public health assessment guidance manual that emphasizes reaching out for the views of communities near superfund sites; created an office of Community Involvement Liaison and established community action panels at many superfund sites; obtained outside peer reviews of a sample of new health assessments completed each year, which have generally validated its efforts; systematically re-examined and updated all the health assessments that it had initially labeled as draft or preliminary; and held public workshops on the health-assessment process throughout the country. ATSDR also has issued about 4,000 health consultations annually, trained more than 20,000 medical and environmental health professionals, and disseminated more than 150,000 pieces of environmental training materials. In addition, ATSDR has become a national leader in exploring the complex relationships between public health issues and environmental equity.[5]

* James Baller is the senior principal of the Washington law firm of Baller Hammett P.C., and Dr. George L. Carlo and Kelly Sund are, respectively, chairman and associate director of research of Health & Environmental Sciences Group Ltd., a Washington-based consulting firm. The opinions in this article are solely those of the authors and do not represent an editorial position by The Bureau of National Affairs, Inc., which welcomes other points of view.

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Based on its experience over the past six years, particularly in fiscal 1992, ATSDR has recently made several noteworthy findings about the potential health risks posed by hazardous waste sites.[6]

ATSDR reported these finding at its first international congress on the health effects of hazardous waste, which more than 900 persons attended, and in testimony before Congress.[7]

Of the 233 sites that ATSDR studied in fiscal 1992, it classified 35 percent as "Public Health Hazards," at which long-term human exposures to hazardous chemicals had occurred or were likely to occur at levels sufficient to cause adverse health effects; 41 percent as "Indeterminate," where insufficient data existed to determine whether human exposures had occurred; and 22 percent either as "No Apparent Public Health Hazard," where, based on current data, prior exposures were no longer of public health concern, or as "No Public Health Hazard," where no exposures had occurred or were likely to occur.

ATSDR's classifications in fiscal 1992 are particularly instructive when contrasted with the results that ATSDR derived by using data concerning all 1,287 sites covered by ATSDR's 1,607 health assessments, since the larger data base was heavily influenced by ATSDR's earlier health assessments. Thus, the percentage of sites that ATSDR classified as "Public Health Hazards" in fiscal 1992 (35 percent) was about double the percentage of all 1,287 sites to which ATSDR had given that classification (18.9 percent), and the percentage of sites that ATSDR classified as "No Apparent Public Health Hazard" or "No Public Health Hazard" in fiscal 1992 (22 percent) was about double the percentage of all 1,287 sites that ATSDR had classified that way (10.4 percent). These results indicate that ATSDR has improved its methodology for identifying or ruling out potentially harmful exposures in a way that is not biased in either direction.

In view of ATSDR's progress in recent years, the notion that ATSDR is unresponsive to community concerns may well be outdated and exaggerated. Indeed, as indicated, ATSDR now has completed more than 1,600 public health assessments. Given the great importance that communities living near superfund sites naturally attach to their health concerns, a truly unresponsive ATSDR would surely have been the target of much more widespread and vocal criticism than it has received.

Fundamental Differences Between EPA, ATSDR

Implicit in the Senate committee's action is the assumption that EPA already does, or can do, what ATSDR does in the health assessment process. In fact, the missions, approaches, and philosophies of EPA and the Public Health Service are completely different, and eliminating the contribution to the superfund process that PHS now makes through ATSDR would have serious adverse consequences for public health.

First, although EPA has a critical role to play in protecting human health, its perspective is fundamentally different from that of PHS. EPA's major statutory responsibilities are to promulgate and enforce environmental regulations and to ensure that releases of toxic chemicals are properly remediated. As a result, EPA focuses on developing standards of general applicability that are intended to err conservatively on the side of protectiveness. In essence, the operative question in EPA's approach is, "What level of exposure is likely to be safe or carry minimal public health risk?" At the same time, in its quest for standards that can be administered by a variety of federal, state, and other parties at sites across the nation, EPA must rely heavily on universal, quantitative models and methodologies that rely heavily upon conservative default assumptions. In short, EPA concentrates on eliminating the sources of perceived risks to human health—a practice known in the public health community as "primary prevention"—relying on the tools that it believes to be most suitable to that specific purpose.

As EPA candidly recognizes in its human health assessment guidance documents, public health issues are beyond the scope of EPA's authority and expertise. EPA thus cannot itself give the public a complete and balanced understanding of the public health implications of toxic chemicals. Public health is the domain of PHS.

In contrast to EPA's regulatory approach, ATSDR's public-health orientation requires it to focus upon identifying and responding to the actual human health effects of hazardous substances on specific populations. For this purpose, ATSDR does not favor mathematical models but makes use of a far broader range of tools than EPA uses, including, where necessary and appropriate, instruments of "secondary prevention" (e.g., surveillance and creation of registries) and "tertiary prevention" (e.g., treatment and rehabilitation). In public health, the operative question is, "What level of exposure presents danger or unreasonable risk to a particular population?" When such a danger or risk has been identified, the appropriate preventive or corrective intervention measures can be determined and implemented.

Matching Remedy To Problem At Hand

Also unlike EPA, ATSDR does not favor permanent or comprehensive remedies if lesser remedies will be more timely and effective in protecting the health of particular populations. Although EPA's approach to remedy selection may change to some extent if certain proposals currently under consideration are enacted, erring on the side of conservatism and overprotectiveness has always been, and will continue to be, an institutional imperative for EPA, an essential part of its job for which it makes no apology. By contrast, ATSDR is steeped in the public health tradition of matching the remedy to the specific problem at hand. ATSDR also is obliged to prefer remedies that intrude as little as possible on the lives of affected populations because invasive remedies can often themselves cause injury to public health.

Also in contrast to EPA, ATSDR is responsible solely for human health issues and is not subject to pressure to make decisions that are driven in part by ecological and other considerations that are not directly related to human health. As such, ATSDR can make an important contribution in helping to evaluate the human health consequences of the choices available to EPA. This is not to denigrate non-health concerns or to suggest that EPA, too, should concentrate only upon human health. But EPA and the public can make rational decisions about costs and benefits only if EPA risk managers and the public have sufficient information to evaluate the individual elements of perceived risks that EPA would regulate.

Furthermore, in exercising its duty to protect and promote public health, ATSDR also is likely to be more attentive than EPA to the possible damage that inappropriate communications of risk may cause to public health. On one level, misstatements of risk can have direct adverse effects on the mental and physical health of affected populations. For example, when government officials misreported the risks of birth defects associated with releases of dioxin in Seveso, Italy, scores of women aborted their pregnancies unnecessarily. Closer to home, worries about personal health, the well-being of children, plunging property values, etc., could well have similar adverse public health effects. On a broader level, misstatements of risk that unduly upset the public.

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legislators, and regulators can result in a serious misallocation of society's resources to address more significant threats to public health. ATSDR's involvement in the superfund process minimizes the potential of harm to public health from incorrect or insensitive communications of health risks.

Consequences In Particular Cases

The fundamental differences between EPA and ATSDR can have very significant consequences in particular cases, as the following three examples illustrate. First, at the Smuggler Mountain, Colo., superfund site, EPA found elevated levels of lead in the soil and, driven by its conservative mathematical models, concluded that a multimillion-dollar remedy of excavating and removing the contaminated soil was necessary. In response to community concerns about the potential adverse health effects of EPA's remedy, ATSDR tested the blood levels of children living near the site and determined that EPA's remedy was unnecessary. ATSDR also determined that EPA's remedy would actually increase health risks to the community by stirring up lead dust.

Second, after years of negotiation at the Brio Refining site in Texas, EPA and the principal responsible party agreed that incineration would be the appropriate remedy for the contamination present at the site. Called in late in the process at the urging of the community to review this remedy, ATSDR opposed it. Had ATSDR been consulted earlier, it might well have helped the parties select a remedy that was acceptable to all concerned.

Third, in response to community concerns about the potential adverse effects of hazardous chemicals at the Forest Glen, N.Y., site, ATSDR issued a public health advisory on which EPA relied heavily in listing the site on the National Priorities List and thereafter relocating much of the community on or near the site. EPA would not otherwise have been able to take this action, as the site did not qualify for listing on the NPL on the basis of its score under EPA's Hazard Ranking System.

In each of these examples, ATSDR's involvement had a major impact. But for ATSDR, EPA would have adopted a remedy in one case that was unnecessary and actually more dangerous to the community than a far less expensive remedy; it would have gone forward with a remedy in the second case that may not have been protective enough; and it would have been blocked by its own ranking system from acting at all in the third case. As these examples also show, ATSDR was indeed responsive to community concerns; in fact, ATSDR was more responsive than EPA in two of the cases.

In short, EPA and ATSDR have complementary and essential, but very different, roles to play in the superfund process. Giving EPA sole authority to conduct health assessments and eliminating the public health perspective that ATSDR brings to the table would significantly damage the superfund process, often to the detriment of the very communities that the Senate committee seeks to protect.

Recommendations Of National Commission On Superfund

During the current debate on reauthorizing superfund, virtually all concerned have agreed that two of the key goals of the program—although not the only ones—should be to ensure that releases of toxic chemicals from superfund sites do not adversely affect the health of persons living near the sites and to respond to the health needs of persons whose health has been damaged by exposures to hazardous substances. Toward that end, the National Commission on Superfund, representing a broad consensus of industry, environmental groups, labor, academia, and state and local governments, issued a report last winter that, among other things, explored ASTDR's role in the superfund process.

In Chapter 5 of its report, the commission noted that several commissioners had expressed concern that ATSDR had not been effective in achieving its mission. In large part, the commission added, this was due to inadequate funding and to EPA's control of ATSDR's budget. Some commissioners, the report continued, also had observed that ATSDR lacks skill in working with communities and responding to community concerns. Although acknowledging there was evidence that ATSDR had improved in recent years, the commission expressed concern that the agency's reputation was restricting the trust among communities that it needs to be effective.

Ultimately, the commission recommended that Congress designate and fund—independently of EPA—a scientifically based health agency within the Department of Health and Human Services that would have sufficient resources to do the work that ATSDR now does and, in addition, would have response capabilities modeled after the program run by the Center for Disease Control and Prevention to address infectious diseases. The new agency, the commission added, should have strong relationships with the technical experts within the department and with local entities, including state public health agencies and new community work groups. For these and other reasons, the commission concluded the new agency should be either a reformulated ATSDR or a new entity within the department intended to replace ATSDR.

Significantly, the commission not only rejected the idea of transferring ATSDR's health assessment responsibilities to EPA, but it expressly found that EPA's control of ATSDR's budget had been a primary source of ATSDR's credibility problems with certain community groups.

Administration's Bill

In response to the commission's report, the Clinton administration introduced bills in both the House (HR 3800 in its original form) and Senate (S 1834 in its original form) that would give effect to the coalition's major recommendations. In these bills, the administration opted not to replace ATSDR but to shore up its weaknesses and expand its responsibilities.

Although disputes rapidly emerged on other significant features of the administration's bill, virtually no disagreement on the administration's plan to improve ATSDR emerged until the Senate Environment and Public Works Committee introduced its markup vehicle July 28, less than a week before the committee voted on the measure. By then, both the House Energy and Commerce Committee and the House Public Works and Transportation Committee had voted to strengthen and expand ATSDR.

The House Public Works and Transportation Committee's approval of HR 3800 is particularly instructive because it dealt directly with the ATSDR's alleged lack of responsiveness to community health concerns. Rather than eliminate ATSDR's role in the health assessment process, the committee voted in Section 107 of its bill to require ATSDR to work "actively" with community working groups in gathering data, designing health assessments so as to take local needs and conditions into account, and reviewing health assessment designs.

Conclusion

Our nation cannot afford to squander its limited resources on remedies that are unnecessary or protective beyond a reasonable margin of safety. All concerned—particularly industry—therefore have a strong interest in ensuring that the agency responsible for performing public health assess-

ments is independent, scientifically based, and credible to affected communities. After all, unless communities trust the agency and its processes, they will never accept the agency's assurances that concerns about public health are unwarranted or that, if problems exist, they can be addressed safely in some cases through measured responses that stop short of comprehensive or permanent remedies.

Has ATSDR irretrievably lost its ability to play such a role? We believe not. Rather, the evidence suggests that ATSDR's credibility with communities is not nearly as low today as the Senate Environment and Public Works Committee may have supposed and that any lingering problems that ATSDR may have from the past can be overcome by measures of the kind that the National Commission on Superfund recommended and that the House committees have incorporated into HR 4916.

But even if ATSDR's reputation with community groups were truly beyond repair, it would be a serious mistake to give EPA exclusive authority over the health assessment process That is a role for which EPA is ill-suited, and experience has shown that a public health agency at EPA's side materially improves the superfund process. If Congress concludes that ATSDR must go, it should embrace the commission's alternative suggestion and establish a new entity within the Department of Health and Human Services that would have sufficient resources and independence from EPA to fulfill ATSDR's mission.

Notes

[1] PL 95-510 (Dec. 11, 1980), as amended by the Superfund Amendments and Reauthorization Act of 1986, PL 99-499 (Oct 17, 1986) codified together at 42 USC 9601, et seq

[2] For a more detailed history of ATSDR, see Baller, Carlo, and Sund, "The Agency for Toxic Substances and Disease Registry A Growing Power in the Hazardous Waste Arena," 21 ER 1951 (BNA) (March 1, 1991)

[3] Congress also broadly expanded ATSDR's authority to conduct scientific research, rank hazardous substances, develop toxicological profiles, identify and fill data gaps, and perform various educational functions.

[4] Approximately 80 percent of the sites on the National Priorities List are located in these 22 states.

[5] ATSDR also has initiated numerous follow-up, health-effects studies, established several exposure registries, ranked the top 275 hazardous chemicals found at sites on the NPL, prepared toxicological profiles for most of these substances identified and sought to fill scores of priority data gaps, and conducted numerous special studies

[6] For greater detail, see Johnson, Baller, and Carlo, "What You Need to Know About ATSDR's Role In the Superfund Decision-Making Process," *Washington Legal Foundation Legal Backgrounder* (Aug. 6, 1993).

[7] M.Y. Lichtfeld, "Public Health Related Findings at U S Hazardous Waste Sites," presented at the International Congress on the Health Effects of Hazardous Waste, May 5, 1993, testimony of Barry L. Johnson before the Senate Environment and Public Works Subcommittee on Superfund, Recycling, and Solid Waste Management May 6, 1983.

[8] *Final Consensus Report of the National Commission on Superfund* (Dec. 21, 1993).

STATEMENT OF THE CHEMICAL MANUFACTURERS ASSOCIATION

The Chemical Manufacturers Association ("CMA") appreciates this opportunity to address the Senate Committee on Finance on the financing provisions of S. 1834, "The Superfund Reform Act of 1994."

CMA is a non-profit trade association. Our member companies represent more than 90 percent of the productive capacity for basic industrial chemicals in the United States. The U.S. chemical industry provides 1.1 million high-wage, high-tech jobs for American workers.

For the years 1991, 1992, and 1993, the chemical industry was the leading U.S. exporter with total exports of $45.1 billion in 1993. Regrettably, that fact masks the much more serious and immediate problem that our net trade surplus sharply declined over that same period from $19.2 billion in 1991 to $16.6 billion in 1993. Domestic and international trade in chemicals is under severe pressure because of weak product demand and excess supply in Europe and because of the large expansion of production in East Asia. According to United Nations data, the U.S. share of world exports of chemicals fell from 17.5 percent in 1970 to 13.8 percent in 1993. That represents a decline of more than 21 percent in total worldwide market share. The U.S. chemical industry is fighting desperately to maintain the competitiveness of its products in domestic and international markets and the 1.1 million American jobs that competitiveness supplies.

Our industry is, therefore, under great pressure to keep all our costs, including taxes, in line with those of international competitors. Since the enactment of Superfund, the U.S. chemical industry has paid substantially in excess of $3 billion in Superfund taxes and related costs. In addition, the chemical industry has paid billions of dollars directly to clean up sites and by our contributions through EPA cost recovery actions.

Yet, CMA supports enactment of S. 1834, the Administration's Superfund reform proposal. We believe that the bill's provisions for the allocation of liabilities under a new fair share liability standard, improved remedy selection and settlement options will effectively reduce the endless disputes and litigation that have characterized the Superfund program since its enactment in 1980. Most importantly, we believe this bill will greatly accelerate the actual clean up of the nation's hazardous waste sites.

One important feature of S. 1834 that is central to the bill's accelerated settlement reforms is the provision for funding reimbursements to eligible parties for costs incurred and equitably attributed to orphan shares. In general, orphan share liabilities are those that are attributable to potentially responsible parties (PRPs) that are defunct, insolvent, or otherwise unable to pay their liabilities. Not only does funding orphan share liabilities correct the inequity of compelling one party to pay

damages attributable to another party, it provides the revenues needed for the bill's exemptions for small business and limitation on municipal liabilities.

This legislation would fund the Superfund program by extending the present Superfund excise taxes at existing rates on chemical feedstocks, imported chemical derivatives, petroleum and petroleum products, and the CET for five additional years. These taxes impose a substantial financial burden on the chemical industry. CMA, nonetheless, urges the Committee on Finance to support the Administration's proposal to extend these taxes at existing rates for five additional years.

Over the past few weeks, our members have been greatly troubled by proposals to use the CET which is now pledged to the Superfund trust fund to meet the budget needs of other programs. **CMA is unalterably opposed to using the CET for any non-Superfund purpose.** These proposals are frequently couched in confusing discussions of budget pay-go credits, yet they suggest and imply that these taxes are not needed for the Superfund program which is certainly not correct. The Congressional Budget Office is on record that the Administration's Superfund reform program will require every dollar of these tax revenues. We applaud the Committee on Finance for moving forward the responsible reform of Superfund by holding hearings on this bill.

We believe an important substantive change to the Administration's Superfund reform proposal is needed now to avoid a major future budget problem. Under the Administration's proposal the Superfund program—including the entitlement for the reimbursement of expenses attributable to orphan share liabilities—would be extended through the year 1999, while the Superfund taxes would be extended through the year 2000. New legislation to extend the Superfund program at that time would not have the "budget pay/go" credit needed under Congressional budget rules to offset the cost of extending the entitlement for orphan shares without new or increased taxes or program cost reductions. You can eliminate this problem now by extending both the Superfund program and the Superfund taxes through December 31, 2000.

CMA, therefore, urges that you adopt the Administration's request to extend at existing rates the Superfund excise taxes on chemicals and petroleum and the corporate environmental tax for five additional years to fund the provisions of S. 1834 as reported by the Committee on Environment and Public Works. We strongly support the progress toward responsible Superfund reform in this Congress that this bill represents. The past 13 and 1/2 years of the administration of the Superfund program attest to just how very much these reforms are needed today.

Statement of the National Association of Mutual Insurance Companies

INTRODUCTION

Mr. Chairman and Members of the Committee: Thank you for the opportunity to submit this testimony to the Senate Finance Committee.

The National Association of Mutual Insurance Companies (NAMIC) is the largest property and casualty company trade association in the world with over 1240 member companies. The NAMIC membership comprises nearly 30 percent of property and casualty insurance premiums in the United States. Our membership includes all types of property and casualty insurance companies, including mutuals, stocks, reciprocals, reinsurers and surplus lines carriers. We have a diverse membership with companies ranging in size from small mutuals that only write in one county to very large companies such as State Farm and Nationwide.

THE ENVIRONMENTAL INSURANCE RESOLUTION FUND (EIRF)

Since its introduction in February, NAMIC has had serious concerns about the Environmental Insurance Resolution Fund (EIRF) contained in S. 1834/H.R. 3800, the Superfund Reform Act of 1994. The EIRF would raise at least $8.1 billion from the property and casualty insurance industry over ten years in an attempt to reduce litigation between potentially responsible parties (PRPs) and their insurers over Superfund coverage disputes.

The EIRF unfairly singles out the insurance industry—which did not contribute to the pollution of hazardous waste sites—to provide all of the new finances for Superfund. This money would only be used to address a small part of the problem, to resolve disputes between PRPs and insurers. There is no guarantee that the money from the EIRF will be used to clean up sites. If PRPs would even choose to settle with the EIRF, they could use the money to pay for past legal costs or to subsidize litigation against the government.

We are also concerned about the uncertainty of the EIRF. If, after collecting taxes from insurers and creating an EIRF bureaucracy to verify hundreds of thousands of insurance records, fewer than 80 percent of the PRPs choose to settle, the EIRF would be abolished. This effort would be a tremendous waste of time and resources that would do absolutely nothing to expedite clean up.

NAMIC is also concerned about provisions in the Senate version of the Superfund Reform Act that could substantially increase costs for the EIRF and subsequently increase the tax burden on insurers. One of these provisions is that the selection of state percentages is based on ⅔ venue of current litigation and ⅓ location of Superfund sites rather than the House version of ½ venue, ½ site location. Because PRPs tend to select venue for their litigation based on favorable state law, giving more weight to venue would place more settlements in the 60 percent category, so more money would be needed from the EIRF.

The other substantial change is that interest on past costs would be paid from the date of acceptance of the EIRF offer in the Senate bill. In the House version, interest was not to be paid until the fifth year.

Because the $8.1 billion EIRF figure is based on the House version of the bill, we encourage the Finance Committee to obtain a reading on how much these changes would cost the EIRF and how much additional revenue would actually be required before taking action on the financing portion of this legislation.

EIRF FINANCING PASSED BY THE WAYS AND MEANS COMMITTEE

NAMIC is opposed to the EIRF financing proposal that the House Ways and Means Committee approved on August 19, 1994.

The legislation approved by the Ways and Means Committee would raise $810 million per year from the property/casualty insurance industry over a ten year period. In years one through four, 45 percent of the revenues would come from a retrospective tax on certain commercial premiums of direct insurers written during the period of 1968–1985, 25 percent of the funds would come a retrospective tax on reinsurance premiums for this commercial insurance, and 30 percent would come from a prospective tax on most commercial premiums including fire, commercial multiple peril, other liability, product liability, allied lines, inland marine, commercial auto no-fault, other commercial auto liability, commercial auto physical damage, farmowners multiple peril, ocean marine, financial guaranty, aircraft, fidelity, surety, glass, burglary and theft, boiler and machinery, and others designated by the Treasury Secretary.

In years five through ten, 65 percent of the revenues would come from the prospective tax, 4.4 percent would come from the retrospective tax on reinsurance, 10 percent would come from special assessments on direct insurers having claims resolved by the EIRF, and 20.6 percent would come from assessments on reinsurers having claims resolved by the EIRF.

The original intent of the Environmental Insurance Resolution Fund and the tax on insurers was to offset the reduction in insurers' liability. However, when one carefully examines who will pay the tax, one can clearly see that the total number of companies who are required to pay the tax is far greater than the number of companies who will pay the tax and actually receive a benefit from it.

NAMIC believes that the single most important principle for financing the EIRF should be that those insurance companies that benefit from it should pay most, if not all, of the funds into it. The legislation passed by the Ways and Means Committee moves significantly away from this objective by making a greater proportion of the tax prospective and by extending the tax to lines of business that have absolutely no connection to environmental liability.

The goal of the EIRF is to reduce the number of disputes between PRPs and insurers over whether or not policies such as commercial general liability covered the clean-up of pre-1986 hazardous waste. Theoretically, this EIRF would provide more certainty for the insurers involved in these disputes. Because these disputes involve only pre-1986 sites, it is logical that the tax should apply to only those insurance policies written before 1986. A prospective tax would have no connection to the coverage disputes that are underway and would place an unfair burden on thousands of companies that have never been involved in Superfund litigation.

Records demonstrate that the proponents of prospective financing for the EIRF have reduced their commercial writings since the mid-1980's. Many NAMIC member companies and others helped fill the void of the 1985–86 availability/affordability crisis by picking up these commercial writings over the past several years. By the time these companies picked up these coverages, the industry had become aware of Superfund, and companies had begun either excluding pollution coverage or specifically writing environmental liability coverage and charging appropriate premiums.

Requiring companies who write commercial business today, but have no pre-1986 Superfund liability, to pay taxes to the EIRF is nothing less than a bail-out of those companies who do have the liability.

This situation is exacerbated by the fact that the prospective tax would apply to many commercial lines of business that have never been the subject of environmental coverage disputes nor have the potential to be the subject of these coverage disputes. Some of these lines include commercial auto insurance, surety, glass, and burglary and theft. Also of particular concern is the provision that gives the Treasury Secretary the authority to extend the tax to other lines of business.

Treasury officials have claimed that NAMIC's major concerns have been addressed through the $50 million cumulative exemption for the retrospective and $5 million annual exemption for the prospective tax. While this does help NAMIC's small member companies, about 400 of our medium-sized and large member companies, many of whom have never been involved in Superfund litigation, will pay substantial EIRF taxes under this proposal, especially taking into account the fact that so many lines of business will be subject to the tax.

ACCEPTABLE SOLUTIONS

NAMIC believes that the best course of action at this time would be to delete the EIRF from the Superfund Reform Act. Upon removal of the EIRF, NAMIC would support the other titles of the legislation.

NAMIC believes that the EIRF should be eliminated for the reasons stated at the beginning of this testimony. The EIRF will require a tremendous amount of money from the insurance industry—which did not pollute the sites in the first place—and there is no guaranty that its funds would be used for clean up.

If Congress determines that inclusion of the EIRF is absolutely essential for the passage of Superfund reform, NAMIC urges the Finance Committee to adopt the proposal set forth by the National Association of Independent Insurers (NAII). This proposal would establish a Commercial Insurer Tax upon those property/casualty insurers that write business in the commercial lines that have generally been the subject of environmental coverage disputes. This part would finance 30 percent of the EIRF. The NAII proposal would also establish a Claims Settlement Tax only for those insurers that actually have Superfund claims pending in the EIRF. Each insurer with claims pending in the EIRF would pay a tax equal to its proportional share of these claims. This part would finance 70 percent of the EIRF.

The NAII proposal upholds the important principle that those who benefit from the EIRF should pay the majority of funds into it. NAMIC could support the EIRF if the Congress would adopt the NAII financing proposal.

IN CLOSING

NAMIC urges the Finance Committee to closely examine the merits of the EIRF to determine whether or not an $8.1 billion tax on one particular industry would be worthwhile. NAMIC believes that Congress should reconsider the EIRF or, at the very least, adopt a proposal that would truly require those who would benefit from the EIRF to pay for it.

NAMIC looks forward to working with the Finance Committee to find ways to establish an efficient and equitable funding mechanism for the Superfund program.

STATEMENT OF THE NATIONAL ASSOCIATION OF WATER COMPANIES

The National Association of Water Companies (NAWC) would like to thank the Committee for holding this hearing today to review the financing aspects of the Superfund Reform Act of 1994. We would like to urge the Finance Committee to act quickly on this important legislation and also to include S. 289 as introduced by Senator Reid as a revenue neutral amendment. We believe that inclusion of this amendment will go a long way toward furthering the primary goal of the Superfund Reform Act: namely, that Superfund trust fund monies be spent on clean up of contaminated sites and not on non-environmental expenditures.

NAWC is the trade association representing the nation's investor-owned water utilities. It's more than 370 memmbers in 41 states provide safe, reliable drinking water to over 22 million Americans every day. Our members employ a combined work force in excess of 15,000 and have $9 billion invested in gross plant and equipment. We support the Safe Drinking Water Act, the Clean Water Act, and this Committee's efforts to provide a clean environment to all citizens and to future citizens.

WHAT IS OUR CONCERN?

Since the enactment of the Tax Reform Act of 1986, our members have been collecting federal taxes from the builders of new homes, small town governments, individuals and even the federal and state governments, including the Superfund Trust Fund, for something called "Contributions in Aid of Construction" or CIAC. In addition, because the collection of these up front taxes is considered to be taxable in' come to our members, they must also collect taxes on these taxes. This so-called "gross up" can result in the total taxes collected for Contributions in Aid of Construction equaling as much as 70 percent of the original CIAC.

WHAT IS A "CONTRIBUTION IN AID OF CONSTRUCTION" OR CIAC?

Water suppliers, like all utilities, are capital intensive businesses. Historically, they have received the capital for the construction of a utility extension directly from the customer (typically a home builder, although it can be a public school, a government agency or trust fund like Superfund, or an individual homeowner). The customer contributes this property, or a cash equivalent, to the utility. In this way, utilities can eliminate the need to spread additional borrowing costs, in the form of rate increases, to the existing body of customers who are already paying for the infrastructure.

It is important to keep in mind that privately owned water suppliers are highly regulated by state utility commissions. Almost all state commissions share two general philosophies about our business. First, they do not allow our members to make a profit from water and sewage main extensions paid for by others. Second, costs associated with hooking up new customers should not be borne by existing customers. With a few exceptions, state commissions require private and investor owned water and sewage utilities to collect up-front from the entity paying the CIAC, any taxes or fees associated with the extension of new service.

WHY DO WE PAY TAXES ON CIAC?

Prior to enactment of the Tax Reform Act of 1986, CIAC was not considered as gross income of an investor-owned utility and therefore was not subject to federal income tax. In addition, utilities could not make a profit from CIAC nor could they take tax depreciation or investment tax credits on CIAC.

The Tax Reform Act repealed section 118 (b) of the Internal Revenue Code and thus subjected CIAC to tax as gross income. This change was done without the benefit of a hearing and was done strictly as a revenue raiser.

HOW IS THE TAX TREATMENT OF CIAC RELATED TO SUPERFUND REAUTHORIZATION?

The purpose of Superfund is to clean-up toxic waste sites. Unfortunately, Some Superfund dollars have gone to paying taxes for CIAC. Many contaminated sites eligible for Superfund money contain contaminated groundwater supplies. Often the only way to solve this problem and assure clean, healthy water supplies for people around the site is to bring in water from one of our member companies. Of course, in the cases where our members provide water service to contaminated sites, Superfund dollars must be used not only to finance the main extensions, but also to pay the taxes and the gross up on the taxes. Please see the list of examples attached to this testimony.

HOW DOES S. 289 SOLVE THIS PROBLEM AND HOW DOES IT COVER ANY LOST REVENUE TO THE FEDERAL GOVERNMENT?

S. 289 restores the pre-Tax Reform Act tax treatment of CIAC to water and waste water utilities. S. 289 pays for restoration by extending the depreciable life of water utility property placed in service after enactment of the CIAC tax repeal from 20 years to 25 years using straight-line depreciation rather than the 150 percent declining balance method.

CONCLUSION

Amending S. 289 to the Superfund Reform Act of 1994 will further the intent of Congress that Superfund dollars be spent on clean up of contaminated sites. The Treasury Department testified last year that it does not oppose our amendment. The NAWC has worked closely with the Committee staff to assure that every concern with the legislation has been addressed. The Senate has passed previous versions of this legislation twice in the last few years. Finally, this amendment is supported by the National Association of Home Builders. We urge the Finance Committee to adopt S. 289 as an amendment to the Superfund Reform Act of 1994.

CIAC TAX EFFECT ON SUPERFUND SITES BY STATE

Illinois:

1. Kankakee County. The cost to mitigate the leak of automobile fuel into a water systems wellfield will cost $1.5 million, plus approximately $1 million in CIAC tax.

New Jersey:

1. South Plainfield, two projects. The cost of the main extensions totaled $311,795, the tax on these contributions totaled $162,133, a cost increase of over 50 percent.
2. Bridgewater. This project cost $186,898, plus an additional $97,187 in CIAC tax.
3. Warren. This project cost $434,871, plus an additional $226,134 in CIAC tax.

*4. Washington and Tewksbury Townships. Main extension to mitigate contaminated wells would have cost approximately $1 million, plus CIAC tax of $600,000. Not a Superfund site, *project canceled due to cost.*

*5. Franklin Township (Laurel Avenue). Main extension to mitigate contaminated well would have cost $100,000, plus CIAC tax of $60,000. Not a Superfund site, *project canceled due to cost.*

6. Hillsborough Township (Route 206/Champlain Road). Contamination at wells cause by industrial facility mitigated at cost of $450,000 plus $250,000 in CIAC tax.
7. Dover Township. Mitigation of 16 wells contaminated by municipal sanitary landfill. Cost to Township of main extension $79,327, plus CIAC tax of $40,869.

California:

1. Chico (Stanley Park). A main extension and treatment facility upgrade to provide an alternative water supply for groundwater contaminated by trichloroethylene cost $972,000. The CIAC tax on this project was $417,844.
2. Chico (Northgrave Avenue). A main extension and treatment facility upgrade to provide an alternative water supply for contaminated groundwater cost $231,620. The CIAC tax on this project was $56,799.

Missouri:

1. Saginaw and Silver Creek (two small towns near Joplin). These towns had private wells replaced with central water service to substitute for groundwater contaminated with trichloroethylene. The cost of the main extensions was $839,817 while the CIAC tax was an additional $277,140.

Indiana:

1. Gary (Lake Sandy Jo). Lake Sandy Jo Superfund site is an old gravel pit and recreation site that was contaminated with chemicals and debris in the 1970s. The Army Corps of Engineers was contracted by the EPA to install water mains to a nearby investor-owned water utility in order to provide potable water to 50 consumers with groundwater contaminated by the Superfund site. The cost of the main extension was $867,972 while the CIAC tax was an additional $509,152.
2. Terre Haute (Ulrich Chemical). To mitigate private wells contaminated by Ulrich Chemical costs approximately $31,000, plus an additional $18,000 in CIAC taxes.
3. Terre Haute (J.I. Case Company). To mitigate numerous wells contaminated by the Case Company costs $166,000, plus an additional $97,000 in CIAC tax. In this case, the company will pass the tax costs onto its existing customers (permitted in Indiana in some circumstances) which contradicts the whole purpose of contributed property which is to shield existing customers from the cost of main extensions to new customers.

Pennsylvania:

1. New Cumberland Army Depot. Centralized water service was provided to residents surrounding the base whose wells had been contaminated by the Army. The cost of the main extension was $57,010, the CIAC tax was $37,393.

*2. National Guard Armory. Although not a Superfund site, a main extension was requested to mitigate for poor groundwater. The National Guard paid $86,595 for construction and $62,926 for the CIAC tax.

* Either not Superfund sites or canceled project.

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