JAN 0 9 2019

DEPARTMENT of ENVIRONMENT and NATURAL RESOURCES

JOE FOSS BUILDING
523 EAST CAPITOL
PIERRE, SOUTH DAKOTA 57501-3182

denr.sd.gov

January 9, 2019

MEMO TO: Jason Hancock, Director, Legislative Research Council

FROM: Steven M. Pirner, Secretary

SUBJECT: 2018 Annual Petroleum Release Compensation Fund Report

As required by SDCL 34A-13-48, please find enclosed the 2016 Annual Petroleum Release Compensation Fund report from the Department of Environment and Natural Resources. Please contact Alan Bakeberg at 773-3769 or Alan.Bakeberg@state.sd.us if you have any questions on the report.

Thank you.

Enclosure

cc: Joshua Shields, Chief of Communications, Governor's Office
Jason Simmons, Policy Advisor, Governor's Office
Hallie Getz, Budget Analyst, Bureau of Finance & Management

DEPARTMENT OF ENVIRONMENT
and NATURAL RESOURCES

JOE FOSS BUILDING
523 EAST CAPITOL
PIERRE, SOUTH DAKOTA 57501-3182
denr.sd.gov

SOUTH DAKOTA DEPARTMENT OF ENVIRONMENT AND NATURAL RESOURCES

2018 ANNUAL REPORT

CURRENT STATUS OF THE PETROLEUM RELEASE COMPENSATION FUND AND AVAILABILITY OF PRIVATE INSURANCE

RECOMMENDATION

The Petroleum Release Compensation Board's recommendation is to continue having the South Dakota Petroleum Release Compensation Fund (PRCF) serve as the primary financial assurance mechanism in South Dakota as that will continue to ensure a level playing field for all owners and operators of regulated petroleum underground storage tanks who must meet the federal financial assurance requirements. In addition to providing the financial responsibility mechanism for federally regulated petroleum underground storage tanks (UST), the PRCF also covers cleanup costs for petroleum tanks that are not required to have a financial responsibility mechanism, such as aboveground petroleum tanks and non-regulated gasoline, diesel fuel, and heating oil tanks. Over the past ten years, 58% of the nearly $6.5 million spent by the PRCF on cleanups has been for petroleum releases at sites that are not required to demonstrate financial assurance.

BACKGROUND

In 1984, Congress enacted federal legislation requiring the US Environmental Protection Agency (EPA) to develop regulations to address the installation, use, and management of petroleum underground storage tanks. The resulting regulations included requirements to upgrade or replace operating underground storage tanks by December 22, 1998. The regulations also required that corrective action be taken if there was a release from an underground storage tank. In response to concerns regarding future unfunded environmental damages, additional federal legislation was enacted, and regulations were adopted establishing federal underground storage tank financial responsibility requirements. Owners or operators of petroleum underground storage tanks were required to demonstrate financial responsibility for taking corrective action and for compensating third parties for bodily injury and property damage caused by releases. Most sites are required to demonstrate financial responsibility of at least $1,000,000 per occurrence.

With the enactment of the federal regulations, private insurance essentially abandoned the pollution liability market in the late 1980s. The insurance industry responded to these requirements by adopting "pollution exclusion" clauses in their policies. With private pollution liability insurance essentially unavailable, most of the underground storage tank owners had few, if any, options for demonstrating financial responsibility.

The South Dakota Petroleum Release Compensation Fund (PRCF) was established by the 1988 Legislature to fill the void left by private insurance, to financially assist tank owners with the cleanup costs of petroleum releases, and to meet the federal and state environmental financial responsibility requirements for regulated underground tank owners. The EPA has approved the PRCF as an acceptable mechanism for tank owners to demonstrate financial responsibility for corrective action and third-party compensation as required by state and federal law. EPA Region 8 further identified the PRCF as a "model program".

The PRCF cleanup coverage is comprehensive in that all petroleum tank sites, including abandoned tank sites and aboveground tank sites, as well as underground storage tanks, are covered. While other methods of demonstrating financial responsibility, such as self-insurance or private insurance, are available to a limited group, the PRCF is the only mechanism that is presently available to every petroleum tank owner or operator in the state.

A five-member advisory board appointed by the Governor makes recommendations on program policies. Revenues are generated by a $0.02 per gallon tank inspection fee on petroleum products received in the state. The fee generates about $17 million per year. In fiscal year 2019 the PRCF will receive $0.004 per gallon of the fee, or about $3.4 million per year, with the balance going to the Ethanol Fuel Fund and the Capital Construction Fund (CCF). SDCL 5-27-6 transfers 64 percent of the CCF deposits to the Water and Environment Fund (WEF). The WEF provides funding assistance for water and wastewater infrastructure projects that protect human health and the environment.

The PRCF provides reimbursement of cleanup expenses and third-party liability claims up to $990,000 ($1,000,000 less a $10,000 deductible). Only necessary and reasonable cleanup expenses incurred after April 1, 1988, are eligible for reimbursement. Reimbursement for third party claims can only be made for certain petroleum releases reported after April 1, 1990. The PRCF also pays for all tank removal and cleanup costs incurred through the Abandoned Tank Removal Program, which was created by the 2000 Legislature (see SDCL 34A-13-49).

In 2005, Congress passed the Energy Policy Act, which included a new requirement that owners and operators of regulated underground storage tanks be trained to reduce spills and leaks. Since 2011, the PRCF has funded storage tank training at various locations throughout the state through a contractor. More than 2,150 people have attended the training, and South Dakota maintains a 99.5 percent training compliance rate for facilities operating underground storage tanks.

AVAILABILITY OF INSURANCE

Pursuant to SDCL 34A-13-48, "the board [Petroleum Release Compensation Board] shall endeavor to integrate private insurance as the primary or secondary risk taker... ". This statute also requires the board to meet at least annually with members of the insurance industry who have registered with the board. The purpose of the meeting is to evaluate the availability of private insurance coverage for petroleum contamination cleanup and third party liability coverage. After meeting with the public on this matter, the board is required to report its findings to the Legislature by January 10th of each year. This year the meeting was held in Pierre, South Dakota on December 13, 2018.

Preparations for the Meeting

In preparation for the meeting, written invitations were extended to members of the insurance industry and associations representing industry groups in South Dakota with a possible interest in the program. This year input was sought from the following representatives of insurance and associations:

- Independent Insurance Agents of South Dakota;
- Western Dakota Insurors;
- Federated Insurance Company;
- National Association of Insurance and Financial Advisors;
- Petroleum Marketers Management Insurance Company;
- South Dakota Truckers Association;
- SD Association of Realtors;
- SD Municipal League;
- SD Bankers Association;
- SD Association of County Commissioners;
- SD Petroleum & Propane Marketers Association;
- SD Association of Cooperatives;
- SD Agri-Business Association; and
- SD Farm Bureau.

Comments from Insurance Industry Representatives

This year, written comments were received from Federated Insurance and Petroleum Marketers Management Insurance Company (PMMIC). The written comments from Federated Insurance indicate that they can provide pollution liability insurance for tank owners who meet their underwriting criteria and who purchase their property and casualty insurance coverage. Federated Insurance indicated there would be certain sites that would not be eligible for coverage due to concerns related to leaking tanks, existing contamination not fully defined, questionable tank or pipe quality, poor tank management practices, or accounts that do not purchase their property and casualty program. The written comments from PMMIC indicate that if South Dakota decides to integrate private insurance as a risk taker, they are interested in providing insurance coverage for petroleum tanks in South Dakota.

Discussion

Since its enactment in 1988, the PRCF has provided more than $90 million for corrective action at more than 4,750 petroleum release sites in South Dakota. With guidance from the five-member citizen advisory board, the PRCF has accomplished this over the past 30 years while reducing annual cleanup costs from a high of nearly $7 million to less than $600,000, and reducing staff from a high of 15 to the current staff of 5. Additionally, over this time period the revenue allocations to the PRCF have been reduced from a high of $0.02/gallon to $0.004/gallon.

Although much of the past and ongoing efforts have been to finance corrective action at old release sites, the PRCF's primary mission continues to be that of providing ongoing financial assurance for federally regulated underground storage tank owners so that they can demonstrate financial responsibility as required by state and federal law. In addition to providing the financial responsibility mechanism for federally regulated petroleum UST owners, the PRCF also covers cleanup costs for petroleum tanks that are not required to have a financial responsibility mechanism, such as aboveground petroleum tanks, and non-regulated gasoline, diesel fuel, and heating oil tanks. As shown in the table below, 58% of the nearly $6.5 million spent by the Fund on cleanup over the past ten years has been for costs associated with sites that are not required to demonstrate financial assurance.

	Non-Regulated Tanks		Federally Regulated Tanks		
SFY	Amount	Percent	Amount	Percent	Total
2009	$340,111	39.3	$525,739	60.7	$865,850
2010	$383,313	53.1	$338,174	46.9	$721,487
2011	$290,996	68.5	$133,949	31.5	$424,944
2012	$557,346	80.6	$134,190	19.4	$691,536
2013	$267,674	53.2	$235,111	46.8	$502,785
2014	$386,490	53.8	$331,436	46.2	$717,926
2015	$295,647	50.3	$291,941	49.7	$587,588
2016	$342,523	57.1	$256,998	42.9	$599,521
2017	$550,546	68.8	$250,235	31.2	$800,781
2018	$303,886	55.1	$247,405	44.9	$551,291
Totals	$ 3,718,532	58.0	$ 2,745,178	42.0	$ 6,463,709

While there has been a significant reduction in claims since the early 2000s, the Petroleum Release Compensation board believes that this trend will reverse in the near future due to the age of the tank systems in South Dakota and new regulations for underground storage tanks. Currently the average age of tank systems in South Dakota is about 25 years. While there are no regulatory or

industry standards dictating or establishing the useful life of a petroleum tank system, the longer tank systems are in service the more likely they are to fail and leak. In addition to the aging tank systems, the Environmental Protection Agency recently enacted new regulations for underground storage tank systems that the State must implement by 2021. These regulations will require many of the existing underground storage tank systems to upgrade certain components, which will likely result in the discovery of petroleum releases that are currently unknown.

In reviewing the letters from Federated Insurance and Petroleum Marketers Management Insurance Company, and considering testimony and discussion at its meeting, the Board recognizes that private insurance may be available for some tank owners who meet qualifications of the insurance companies. However, tank owners not required by regulation to have a financial responsibility mechanism would not likely purchase insurance, and as a result many would not have the financial resources to pay for cleanups when a release occurs. The Board expressed concerns that dual coverage, risk selection practices and the uninsured sites would likely place a greater burden on some operators while shifting proportionally higher financial liability for the higher risk sites to the State. The Board concluded they could find no reason to change its recommendation from last year. The Board saw no advantage to the public or tank owners on going to private insurance to meet the financial assurance requirements for underground petroleum tank owners.