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January 10, 2011

The Honorable Dennis Daugaard  
and  
Members of the South Dakota Legislature  
State Capitol Building  
Pierre SD 57501

Dear Governor Daugaard and Legislators:

On behalf of the Petroleum Release Compensation Fund Board, I am pleased to submit the annual report on the meeting with insurance industry representatives. The annual meeting and report are required by SDCL 34A-13-48 to determine the availability and affordability of private insurance for pollution coverage for petroleum tank owners.

This year, the board received four letters from members of the insurance industry. No representatives of the insurance industry provided testimony at the meeting. In reviewing the letters submitted for the meeting, the board recognizes that commercial insurance is available for new construction and for tank owners that meet qualifications of the insurance companies. However, the board found no reason to change their recommendation from previous years. They see no advantage to shifting to private insurance in order to meet the financial assurance requirements for petroleum tank owners.

Thanks to your support of this important program, the PRCF continues to be one of the most successful state financial assurance funds in the nation. It is the only program designated as a "model program" by the US EPA Region VIII. The PRCF provides affordable and cost-effective benefits to the citizens of South Dakota considering that it is funded with only about 1/5 ¢ per gallon of petroleum brought into the state.

Best regards,

A handwritten signature in black ink, appearing to read "Dennis D. Rounds". The signature is fluid and cursive, with a long horizontal stroke at the end.

Dennis D. Rounds  
Executive Director

cc: Steve Pirner – Secretary, Dept. of Environment and Natural Resources  
Petroleum Release Compensation Fund Board

**South Dakota  
Petroleum Release Compensation Fund**

**2010 Annual Report to Governor Daugaard and the South Dakota Legislature**

**CURRENT STATUS OF THE FUND  
AND  
AVAILABILITY AND AFFORDABILITY OF PRIVATE INSURANCE**

**BACKGROUND**

The South Dakota Petroleum Release Compensation Fund (PRCF) was established by the 1988 Legislature 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. Both state and federal laws require that most owners of petroleum storage tanks be able to demonstrate financial responsibility for pollution cleanup and third-party liability. The US Environmental Protection Agency (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 federal law.

The PRCF had been attached to the Department of Revenue and Regulation since 2003. The program has now been transferred to the South Dakota Department of the Environment through Executive Order beginning in January 2011. A five-member advisory board appointed by the Governor makes recommendations on program policies and acts as a hearing officer in contested case hearings.

Revenues are generated by a \$0.02 per gallon tank inspection fee on petroleum products received in the state. While the fee generates about \$15 million per year, the PRCF only receives 10.65% of the fee, or about \$1.6 million per year, with the remainder going to the Ethanol Fuel Fund and the Capital Construction Fund

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 enacted through SB 197 in the 2000 Legislature.

**CURRENT STATUS OF THE PRCF - JANUARY 1, 2011****Obligations**

Claims in Office Undergoing Review	\$ 8,902
Estimated Remaining Costs for Sites that Have Received Payments	\$ 1,000,000
Estimated Costs for Reported Sites with No Payments Yet	\$ 2,900,000
Estimated Remaining Costs for the Abandoned Tank Program	\$ 600,000
	=====
<b>Total - Estimated Obligations for Existing Releases</b>	<b>\$ 4,508,902</b>

**Year-End Summary**

Fund Balance on January 1, 2011	\$ 3,872,756
PRCF Revenue for 2010 (10.65% of Tank Inspection Fee)	\$ 1,716,314
Amount Paid since Beginning of Program in 1988 (4,301 tank sites)	\$ 82,694,760
Active Cases ( <i>does not include Abandoned Tank Program sites</i> )	133
Closed Cases with All Claims Settled	1,404
Abandoned Tank Removal Program ( <i>number of applications to date</i> )	3,071

**Breakdown of Payments to Date**

<u>Type of Release Site</u>	<u>No. of Sites</u>	<u>Percent of Total Payments</u>	<u>Payments to Date</u>
Commercial Petroleum Marketer	578	45%	\$ 37,517,290
Commercial Co-op Marketer	145	12%	\$ 9,847,436
<b>Subtotal - Petroleum Marketer</b>	<b>723</b>	<b>57%</b>	<b>\$ 47,364,726</b>
Commercial End User	333	14%	\$ 11,647,642
Federal Government	9	<1%	\$ 121,519
State Government	77	2%	\$ 1,758,073
Local Government	145	6%	\$ 5,039,258
Orphaned Tank Sites	174	10%	\$ 7,775,716
Farmers	4	<1%	\$ 65,977
Non-Profit Organizations	12	<1%	\$ 280,559
Residential	1	<1%	\$ 19,909
<b>Subtotal - Other</b>	<b>755</b>	<b>33%</b>	<b>\$ 26,708,653</b>
Abandoned Tank Program*	2,823	10%	\$ 8,621,381
	=====	=====	=====
<b>GRAND TOTAL**</b>	<b>4,301</b>	<b>100%</b>	<b>\$ 82,694,760</b>

\*The sites in the Abandoned Tank Program include all of the types of sites mentioned above except for commercial petroleum marketers and commercial co-op marketers.

\*\* Grand total does not include \$122,515.03 paid in third-party liability claims.

## **AVAILABILITY AND AFFORDABILITY 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 and affordability 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 Fort Pierre, South Dakota on December 9, 2010.

### **Preparations for the Meeting**

In preparation for the meeting, written invitations were extended to the members of the insurance industry who have registered with the board or have expressed an interest in the program. This year, input was sought from the following:

- Independent Insurance Agents of South Dakota;
- Western Dakota Insurors;
- Federated Insurance Company;
- Commerce and Industry Insurance Company;
- Accordia of Minnesota;
- National Association of Insurance and Financial Advisors; and
- Petroleum Marketers Management Insurance Company.

### **History of UST Financial Responsibility in South Dakota**

In 1984, Congress enacted federal legislation requiring the EPA to develop regulations to address the installation, use, and management of petroleum underground storage tanks (UST's). The resulting regulations included requirements to upgrade or replace operating UST's by December 22, 1998. The regulations also required that corrective action be taken if there is a release from a UST. In response to concerns regarding future unfunded environmental damages, additional legislation was enacted and regulations adopted establishing federal UST financial responsibility requirements. Owners or operators of petroleum UST's 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 for at least \$1,000,000 per occurrence.

With the enactment of the federal financial responsibility requirements, private insurance essentially abandoned the pollution liability market in the late 1980's. 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 state's UST owners had few, if any options for demonstrating financial responsibility.

In response, the 1988 South Dakota Legislature enacted emergency legislation by passing HB 1253 to create the Petroleum Release Compensation Fund. The PRCF filled the void left by private insurance by providing pollution coverage to all UST owners at the level required by the EPA. The EPA approved the PRCF as a suitable method of financial assurance for corrective action and third-party liability for owners of all new and upgraded petroleum tank systems where coverage is allowed by SDCL 34A-13. The EPA Region VIII further identified the PRCF as a "model program". No additional pollution liability insurance or other method of demonstrating financial responsibility is required by petroleum tank owners in South Dakota.

The PRCF cleanup coverage is comprehensive in that all petroleum tank sites, including abandoned tank sites and aboveground tank sites, as well as UST's, 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 regulated tank owner or operator in the state.

#### **Comments from Insurance Industry Representatives**

This year, written comments were received from Pat Rounds (Petroleum Marketers Management Insurance Company); Brian Bowker (Independent Insurance Agents of South Dakota); Kelli Fuhrmann (National Association of Insurance and Financial Advisors) and Eric Lehrer (Federated Insurance).

#### **Discussion**

Since its enactment in 1988, the PRCF has provided over \$82 million for corrective action at 4,301 different petroleum release sites. The current estimate for future costs on known release sites is about \$4.5 million. While much of the past efforts have been to finance corrective action at these old release sites, the PRCF's mission continues to be that of providing ongoing financial assurance for tank owners so that they can demonstrate financial responsibility as required by federal law and in removing orphaned underground tanks and non-regulated tanks that are no longer in use.

In reviewing the letters from Pat Rounds, Kelli Fuhrman, Brian Bowker and Eric Lehrer and considering comments and discussion at their meeting, the board recognizes that commercial insurance is available for new construction and for tank owners who meet qualifications of the insurance companies. However, the board agreed that they could find no reason to change their recommendation from last year and that the PRCF was not in a position to change anything. They see no advantage of going to private insurance to meet the financial assurance requirements for underground petroleum tank owners.

#### **Recommendation**

The Board's recommendation is to continue the program under the same process that is presently in place. While over 1,404 petroleum tank sites have been cleaned up in the PRCF's regular program with all claims settled, there remain over 134 sites with ongoing or pending cleanups. Presently, the PRCF is funded with only a small percentage of the tank inspection fee, which amounts to about 1/5 ¢ per gallon of petroleum that is brought into the state.