

# Environmental Insurance and Risk Management Tools in Brownfields Cleanup and Redevelopment

**Disclaimer:** *This presentation is the compilation of input by multiple insurance industry representatives. Information does not reflect the views of the U.S Environmental Protection Agency.*

# Overview

- Risk management approaches to brownfields cleanup and redevelopment
- Historical context of environmental insurance coverage
- Common environmental insurance policies for brownfields
- Negotiating environmental insurance coverage
- Selecting an insurance carrier
- Premium costs and claims payments
- Public sector roles in environmental insurance

# Risk Management – Goals of Key Players

As in any real estate transaction, the goals of players in brownfields cleanup and redevelopment projects are not always aligned.

## ■ Seller

- Timely sale of property
- Maximize price
- Relief from future liability

## ■ Buyer

- Timely purchase and redevelopment
- Limit liability
- Maximize resale value and flexibility

# Risk Management – Goals of Key Players

## ■ Lender

- Not assume any environmental liability
- Maximize chance of repayment
- Maximize resale value if foreclosure occurs

## ■ Tenant

- Conduct business without interference or exposure to liability for environmental cleanup and/or from employee claims

## ■ Environmental Regulatory Agencies

- Cleanup conducted to a level that protects human health and the environment

## ■ Land Use Regulatory Agencies (Redevelopment Agency)

- Achieve maximum economic, social, and environmental benefits from reclamation and reuse

# The Range of Risk Management Tools

## ■ Due Diligence

- Conduct All Appropriate Inquiry
- Understand pre-existing conditions, risks, and potential impacts on development

## ■ Contractual Protections

- Indemnities
- Representations and warranties
- Covenants

# The Range of Risk Management Tools

## ■ Financial Tools

- Escrow accounts
- Purchase price adjustment
- Grants and loans
- Tax benefits

## ■ Regulatory Protections

- Federal and state statutory protections
- No Further Action Letters or other determinations

## ■ Environmental Insurance

# Limitations of Risk Management Tools

## ■ Due Diligence

- May later prove to have been incomplete
- Science evolves

## ■ Escrows

- Actual costs may exceed escrowed amount

## ■ Indemnities/Representations/Covenants

- Willingness to execute due to financial or legal risk

# Limitations of Risk Management Tools

## ■ Regulatory Protections

- Change in standards
- Exclusions
- “Re-opener” authority in case of threat to human health or environment

## ■ Environmental Insurance

- Availability
- Cost
- Self liquidating
- Exclusions
- Limited term and renewal conditions
- Dollar limits of liability

# Historical Context of Environmental Insurance Coverage

- Coverage for environmental liabilities originated in Comprehensive General Liability (CGL) Insurance
  - CGL insurance provides broad protection against situations in which an entity must defend itself against lawsuits or pay damages for bodily injury or property damage from third party claims
  - CGL contracts are enforced and interpreted based on state law
  - CGL insurance has become more restrictive over time; therefore, it rarely covers environmental liabilities

# CGL and Current Environmental Insurance Policies

## ■ CGL Environmental Coverage

- Broad coverages written by underwriters without environmental expertise
- Environmental regulatory climate rapidly evolving
- Coverage restricted
- Limits low in relation to the exposure
- Premiums and deductibles not closely tied to environmental risk

## ■ Current Environmental Insurance Products

- Underwriters are experienced environmental professionals
- May provide protection for regulatory uncertainty
- Coverage designed specifically for environmental conditions and tailored to each site
- Limits up to \$100 million available
- Premiums and deductibles closely linked to environmental risks

# Environmental Insurance Policies for Brownfields

- Policies are individually tailored for each project
- Principal coverage types\* include:
  - Pollution Liability (PL)
  - Cost Cap (CC)
  - Secured Lender (SL)
  - Finite Risk (FR)
- Policy holders can include buyers, sellers, and intermediary owners (e.g. redevelopment authorities)
- Most are “claims made” not “occurrence” based, requiring claims to be filed during the policy period

*\*Insurance companies use different names to refer to these general types of coverage*

# Pollution Liability

- Third party claims for bodily injury, property damage, and cleanup costs, off-site and on-site
- Newly discovered contaminants
- Natural resource damage claims
- Diminution of property values
- Business interruption due to contamination
- Regulatory re-openers
- Transportation
- Project delay (before or after construction)
- Average term of 1 - 5 years, but up to 10 years can be purchased

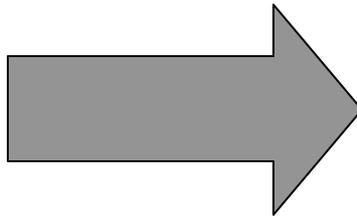
# Cost Cap

- Cost overruns for remediation expenses
- Changes in regulatory standards/laws
- Costs due to newly discovered contaminants or more known pollutants – on-site and off-site
- Based on cost estimates for completing approved remedial action plan
- Policies often require a self-insured retention (SIR) threshold that insured must pay before coverage is applied
- SIR required is usually a function of estimated cleanup costs (e.g. 10%)
- Generally policy period reflects anticipated length of cleanup

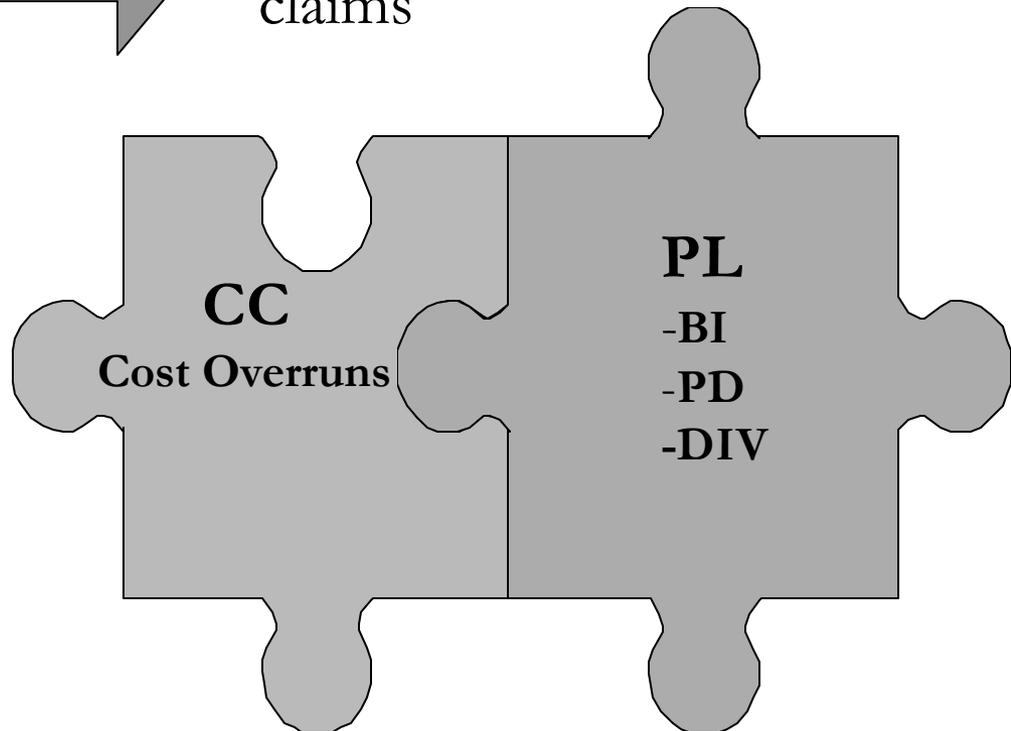
# Policy Example

Developer is interested in building residential units on a brownfield, but has concerns to be addressed before going forward:

- cost-overruns for remediation
- unknown contamination
- third party claims for bodily injury (BI), property damage (PD), and diminution of property value (DIV)



Policy placed for 10 years providing a **Cost Cap** for cost-overruns and a **Pollution Liability** to protect against third party claims



# Secured Lender

- Policy pays for covered loans upon loan default where pollution conditions exist
- Policy can pay for :
  - Loan balance
  - Cleanup costs
  - Legal defense
  - Contract damages
  - Bodily injury/property damage
  - Business interruption/extra expense

# Finite Risk

- Transfers financial liabilities from the insured to an insurance carrier
  - Insured pays the insurer the entire present value of the projected cleanup cost when the insurance is obtained
  - Insurer takes on the financial responsibility for the cleanup
  - Term is negotiable but is typically issued for more costly cleanups lasting more than 5 years
  - May return funds plus interest to insured if funds are not depleted by cleanup

# Negotiating Environmental Insurance Coverage

## ■ Key Players

- Insurance broker with expertise in environmental insurance products
- Insured's legal counsel/environmental attorney
- Environmental consultant
- Insurance company underwriter
- Legal counsel for insurance company

# Negotiation Considerations – Skilled People, Complete Information & Understanding Options

## ■ People

- Brokers, attorneys, and risk specialists with environmental insurance and risk management experience who are involved early in the process
- Regulators available to answer questions and speak to the status of the property and cleanup plans

## ■ Information Needed by both the Insurer and Insured

- Critical environmental information about the property, particularly information as to remedy and cost
- Contractual arrangements and any regulatory agreements
- Nature of the risks to be insured and the trigger points at which coverage will respond

# Negotiation Considerations – Skilled People, Complete Information & Understanding Options

## ■ Understanding Options

- Ability to adapt environmental insurance policies to each individual “site” or “deal”
- Potential to combine policies with indemnities, contractual obligations, guarantees, bonds, and other tools to manage financial and legal risk
- Understanding of whether premium and deductible costs are appropriately priced given the coverage that is needed

# Selecting an Insurer

- Commitment/availability of resources
- Financial strength and rating
- Specialization in environmental insurance
- Claims payment history, to the extent information is available
- Years in the environmental insurance market
- Experience providing the type(s) of coverage required
- Coverage and policy terms available
- Pricing

# Premiums Costs and Claims Payments – The premium is a function of...

- Policy dollar limits and policy term
- Self-insured retention assumed (threshold the insured must pay before the policy starts to pay)
- Stage of remediation
- Size of the site or deal
- Level of characterization and due diligence
- Level of regulatory agency oversight/involvement
- Portfolio vs. single property
- Level of competition
- Future site use and surrounding occupancies
- Expected remedial costs and degree of volatility

# Claims: Process and Considerations

- Insured submits claim
- Insurer acknowledges in writing receipt of claim, assigns a claim number, and assigns a claims adjuster
- Claims adjuster issues letter accepting coverage, declining coverage, or accepting coverage with a reservation of rights
- Second letter typically cites policy provisions to support position taken by insurance company
- Only anecdotal information is available about environmental insurance companies' claims records
  - Environmental insurance policies are still fairly new
  - No body of case law exists as there does for policies which pre-date these policies (e.g., CGL policies)

# The Public Sector and Insurance

- **State sponsored programs**

- Programs in place: Massachusetts and Wisconsin
- Programs in development: California and Wisconsin's new program

- **Local government intervention**

- Risk pooling and portfolio approaches where insurance may not be available for sites with individual cleanup costs under \$1 million, but could be feasible for multiple publicly-owned sites

- **EPA Brownfields Grant funding**

- Recipients of assessment, cleanup revolving loan fund or cleanup grants can use a portion of the grant to purchase insurance
- State and tribal response program funding can also be used for
  - purchasing or developing insurance programs
  - developing risk sharing or indemnity pools

# Links to Additional Information

- Environmental insurance and Brownfields:
  - [EPA Brownfields Program Web page](#)
  
- State environmental insurance information:
  - [\*State Brownfields Insurance Programs, 2004 - Northern Kentucky University\*](#)
  - [Massachusetts](#)
  - [Wisconsin](#)
  - [California](#)