

## **Cost and Risk Allocation Strategies for Brownfield Sites**

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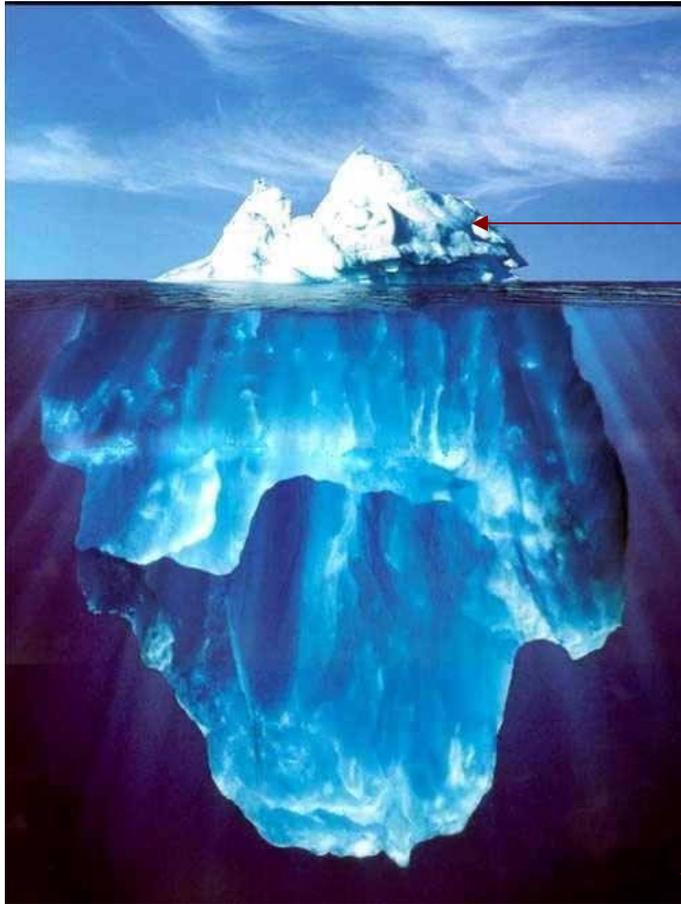
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# Real Estate Trends...

- \$1-2 trillion in commercial properties in the US - 50% estimated to have some contamination
- Corporations are more willing to market legacy properties and share in redevelopment efforts
- Certain lenders, developers and real estate investors have evolved to be more tolerant and understanding of environmental risk
- Recent regulatory developments are making the sale, purchase and redevelopment of contaminated property more attractive
- Infill projects and urban revitalization trends are “hot” in certain markets where environmentally challenged properties are located

# Account for Real or Perceived Liabilities



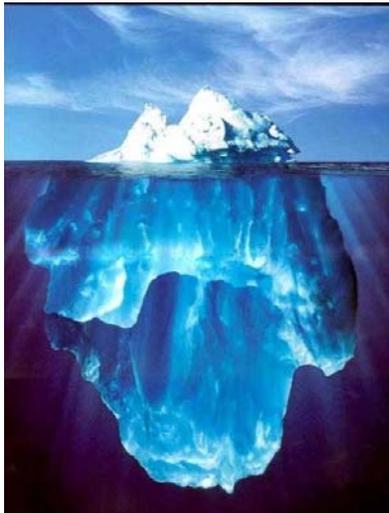
Clean Market Value or  
“Perfect Project” Cost

Environmental Liabilities

Risk

Project Delay Costs

# The Impact of Real or Perceived Liabilities



- Decrease marketability and direct property values
- Complicate conventional financing options
- Delay and complicate site development and use
- Slow and potentially jeopardize future sale or development
- Introduce potential for regulatory and 3rd party legal liabilities
- Costly environmental cleanups may be incurred

# Getting Comfortable with the Risk

## Identify the liabilities:

- Complete environmental due diligence process
  - Initial Assessment to **identify** concerns
  - Investigations to determine the **presence** or **absence** of contamination and **nature** and **extent** of contamination
- At the end of the day you should be able to answer
  - How much is this going to cost?
  - How is it going to be remediated?

# Getting Comfortable with the Risk

## Manage the liabilities

- Lender wants
  - Not to assume any environmental liability
  - Maximize chance of repayment
  - Maximize resale value if foreclosure occurs
- Tenant wants
  - Conduct business without interference or exposure to liability for environmental cleanup and/or from employee claims
- Environmental Regulatory Agencies wants
  - Cleanup conducted to a level that protects human health and the environment
- Land Use Regulatory Agencies wants
  - Achieve maximum economic, social, and environmental benefits from reclamation and reuse

# Getting Comfortable with the Risk

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## Risk/Cost Allocation Strategies

- Escrow accounts
- Price reduction
- Private party contractual protections
  - Indemnities, Representations and warranties
- Insurance
  - Use as a cost recovery source
  - As a product to manage risk

# Using Insurance for Cost Recovery

- Environmental liabilities that arise out of past business operations on a site may be offset by insurance coverage purchased at the time the worst pollution was taking place.
- Usually this is via the comprehensive general liability (CGL) on policies written from 1945 through 1985.
- The CGL form was first written in 1940 and had a very broad scope. The insuring agreement of such policies provided coverage for “bodily injury” and/or “property damage” resulting from an “accident.” Most courts that have considered old “accident” policies have found that policies issued from 1940 to 1966 cover pollution damage resulting from gradual causes.

# Insurance Products to Manage Risks

Pre-1972  
No Pollution  
Exclusions



1972-1985  
“Sudden and Accidental”  
Pollution Exclusion



1986-Present  
“Absolute” Pollution  
Exclusion



# The Market Has Changed

Insurance carriers today

XL, AIG, CHUBB, ACE, Zurich, Liberty, Ironshore & Navigators

- Coverage's have broadened.
- Premiums have fallen greatly.
- Risks are better defined.
- Flexibility in terms

# Key Types of Environmental Insurance

Environmental risks arise from:

- Known and unknown problems from past pollution incidents
- Potential pollution incidents in the future

Products address several types of risks including:

Category	Product
<b>Property related environmental risks</b>	<ul style="list-style-type: none"><li>• <b>Pollution Liability insurance</b></li><li>• <b>Mold and UST insurance</b></li></ul>
<b>Contracting/consulting risks</b>	<ul style="list-style-type: none"><li>• <b>Contractors Pollution liability</b></li><li>• <b>Errors and Omissions</b></li></ul>
<b>Cleanup projects and legacy liabilities</b>	<ul style="list-style-type: none"><li>• <b>Remediation cost cap</b></li><li>• <b>Liability buyout</b></li></ul>

# Pollution Legal Liability - PLL

4Bodily Injury on and off site

4Property Damage on and off site (DIV)



On-site cleanup coverage for contaminants on, within or under the site

## Timeline of Coverage\*



Covers Unknown  
Pre-existing  
Contamination

Policy Inception

Covers Ongoing  
Pollution Events

\* Discovery or Third-Party Trigger

# Environmental Insurance - How It Works

- **Pollution Legal Liability**

- Third Party Claims for Bodily Injury, Property Damage or Cleanup Costs (discovery or 3rd party trigger for cleanup)
  - **From Pre-Existing “Unknown” Pollution Conditions**
  - **From Known Pollution Conditions below actionable levels**
  - **From “New Pollution Conditions (after policy inception)**
  - **On-Site and Off-Site**
- Diminution of Property Values
  - Environmental Stigma
- Natural Resource Damage Claims
- Contractual Obligations
- Project Delay (during construction)



# Environmental Insurance - How It Works

- **Pollution Legal Liability continued:**
  - Bodily Injury –Mental Anguish / Emotional Distress
  - Regulatory Re-openers and Third party risk
  - Business Interruption/Extra Expense (Post-Construction Loss of Use/Rents)
  - Transportation
  - Non-owned Disposal Sites
  - Asbestos, Lead and Mold coverage available
  - Claims-made Forms With Multi-year Terms (1 - 10 YEARS OR MORE)
  - Excess/Failure of indemnity insurance – very popular see next page



# Excess over indemnity – Environmental insurance

THIS ENDORSEMENT CHANGES THE POLICY. PLEASE READ IT CAREFULLY.

## INDEMNIFICATION AGREEMENT TRIGGER

This endorsement modifies insurance provided under the following:

POLLUTION AND REMEDIATION LEGAL LIABILITY POLICY

In consideration of the indicated adjustment of premium, the INSURED and the Company agree to the following Policy change(s):

Premium (increase/reduction): \$ \_\_\_\_\_

Section I, INSURING AGREEMENT, A. Coverage A – POLLUTION LEGAL LIABILITY, B. Coverage B – REMEDIATION LEGAL LIABILITY, C. Coverage C – LEGAL DEFENSE EXPENSE and D. Coverage D – CONTINGENT TRANSPORTATION COVERAGE or any other coverages provided by endorsement shall apply only:

- 1). to matters which arise out of or are subject to the below referenced Indemnification Agreement and obligations thereunder, if, during the POLICY PERIOD, the below referenced Indemnitor fails to perform its obligations under the below referenced Indemnification Agreement and the INSURED first notifies the Company, in writing, of that failure during the POLICY PERIOD, Automatic Extended Reporting Period, or Optional Extended Reporting Period, if applicable. In the event that the Indemnitor fails to perform its obligations under the Indemnification Agreement, the INSURED agrees to assign to the Company all rights of recovery under the below referenced Indemnification Agreement that are specific to the LOSS, REMEDIATION EXPENSE, LEGAL DEFENSE EXPENSE, or any other coverages provided by endorsement and to cooperate with the Company in pursuing recovery against the Indemnitor; or
- 2). to matters which do not arise out of or are not subject to the below referenced Indemnification Agreement and obligations thereunder, subject to the terms and conditions of the Policy.

Indemnitor:

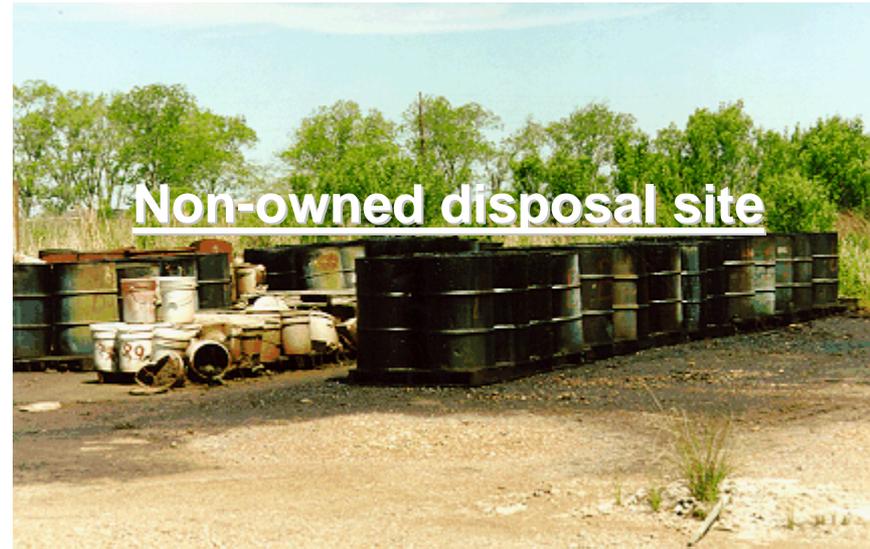
Indemnification Agreement(s):

# Pollution Legal Liability - PLL



## Non-Owned Disposal Site Coverage

- Covers pollution emanating from non-owned site resulting in cleanup costs, property damage, and bodily injury beyond the boundaries of such a site
- Third-party claims for cleanup costs at non-owned locations



# Pollution Legal Liability - How it Works

## Coverage is “claims made” with Multi-year terms

1-10 year term or more

Deductible is “per incident”

## Can Assist as a “Transactional tool”

Replacing – Buyer/Seller indemnification

Prevent or assist with price \$ discounting

Can strengthen indemnification

Replace escrow and hold back provisions

Lender comfort

## PLL Structure Example

**\$ 5 Million per occ. Limit /  
\$ 10 Million agg. limit**

**\$25K Deductible (per incident)**

**Premiums based on site related exposures determined by Environmental Reports, i.e. Phase I/II's**

**Typical Premiums....**

# Lenders Environmental Insurance

Covers “lender only” should the borrower default on loan and a pollution condition is present.

Possible to insure “known pollution conditions” for lender

Less expensive than a PLL

Insurance will pay the lesser of the clean-up costs or remaining loan balance

Assists lender in closing on the tougher transactions

# What if you are responsible for Remediation? The Clean-up Cost Cap Program



# Financial Risks Associated With Clean-up

- The actual contamination can simply be greater than anticipated;
- A missed “hot spot” of pollutants that is discovered in the course of performing a clean-up pursuant to the RAP;
- Off-site clean-up costs can be discovered while remediating the on-site contamination;
- Disposal costs can be higher than anticipated;
- A governmental agency can change clean-up requirements; and
- Remediation design may fail.

# Cleanup Cost Cap — How It Works

## Structure Example

\$2MM Risk Transfer

\$100K Buffer 10%

Projected clean-up cost of \$1MM

**Premium: 10% of projected clean-up cost**

# A few examples of PLL in Action

- Buyer purchasing a strip mall in “as is” condition wanted to protect themselves from claims from contamination former Dry cleaner/ gas station



Policy placed w/\$5M limits for 10 years for \$ 60K Premium with \$25K deductible - includes: BI/PD/Cleanup from pre-existing conditions  
- Bank also comfortable

- Developer wanted to build Condos on “Brownfield” but was concerned with Cost-overruns for remediation – Thorium. Also coverage unknown contamination and third party claims for BI,PD & DIV



Policy placed for 10 years providing a cost cap for cost-overruns of Thorium, and PLL to protect against third party claims for BI, PD, & DIV  
\$20M limits; \$250K deductible  
10 years; \$350K pr

# PLL in Action

- Private Equity Firm acquires Animal nutrition company, required environmental insurance for the deal – with no exclusions in 2 days.



Policy placed w/\$10M limits for 10 years for \$ 150K Premium with \$100K deductible - includes: Clean-up costs from pre-existing conditions & new conditions

- A Manufacturing Company wanted to buy parcel of land, however there was Contamination - BUT the buyer did not want to rely on the sellers indemnification for financial reasons



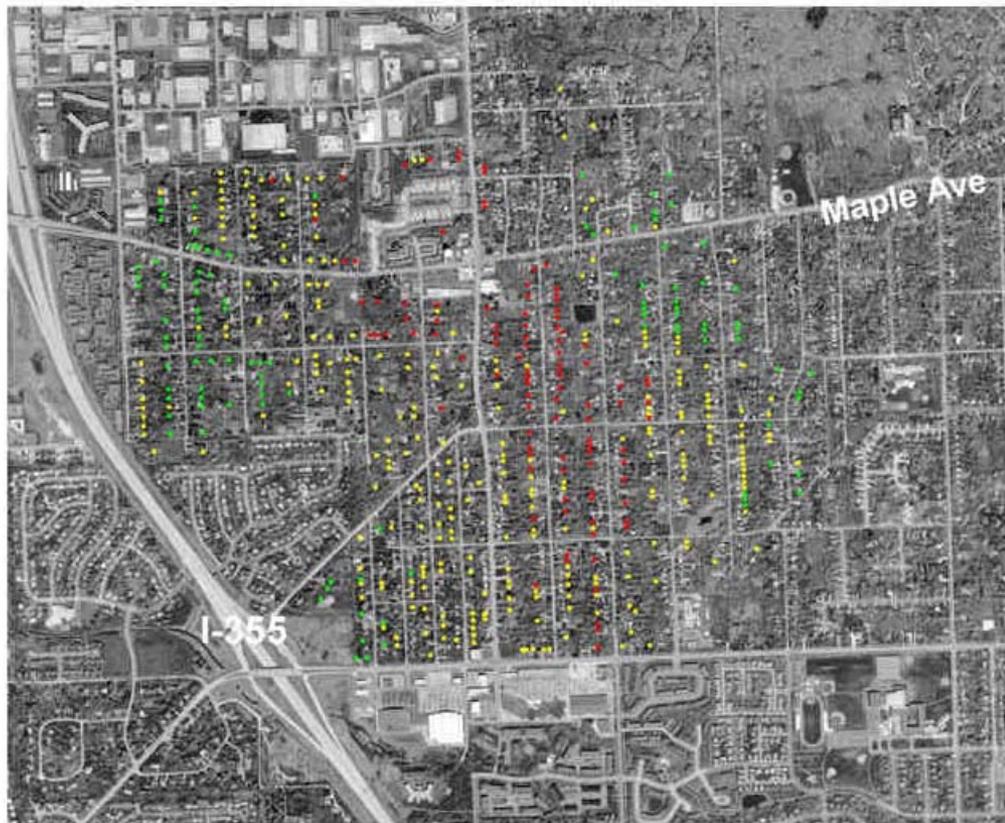
Policy placed w/20M limits for \$200K premium with \$100K deductible. Policy is includes: Excess of the current indemnity for known contamination and covers third party claims (PD/BI/Cleanup) against the new purchasers.

# PLL in action

- A REIT wanted to sell a portfolio of 10 properties to a new buyer. However, the buyer was concerned one of the properties would suffer Diminution In Value due to the Environmental Stigma from the sites polluted past  Policy placed w/\$5M limits over 10 years with \$ 50K deductible for \$100 K Premium. Policy includes Coverage for First and Third party DIV claims, and any third party Bodily injury claims - More importantly made the buyer comfortable, and completed this transaction.
- Sale Leaseback for an Automotive supplier with multiple locations.
- Private equity was the driver.  Policy was placed to insure the known conditions for the benefit of the Buyer. All parties happy, PE, Buyer and tenant
- The sites came with an environmental history and required further remediation – solvents.
  - 5 locations Insured Excess of tenants indemnity \$ 10m limit for 10 years \$ 100K deductible for \$170K premium

# PLL in action

- Site with Known Solvent release – policy excludes remediation of Known contamination, but insured potential third party liability including – Bodily injury claims and Diminution In Value



## Ellsworth Industrial Park Site Downers Grove, Illinois

TCE Concentrations  
in Residential Wells



LEGEND	
TCE Concentration (ppb)	
● Nondetect	
● < 5	
● 5 +	

# How these Two Policies Connect to Form a Solid Wall of Protection



# Questions?

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