

MARSH

GLOBAL ENVIRONMENTAL PRACTICE



Questions & Answers

About Brownfields

On January 11, 2002, President Bush signed into law H.R. 2869, the Small Business Liability Relief and Brownfields Revitalization Act. This landmark legislation is the evolution of financial and legal incentives that began in the 1990s in an effort to help communities clean up and redevelop the estimated 450,000 Brownfield sites across America.

For the first time, the legislation formally defines the term “Brownfield” under the Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA - or “Superfund”), as real property, the expansion, redevelopment, or reuse of which may be complicated by the presence or potential presence of a hazardous substance, pollutant, or contaminant. The new definition includes certain properties impacted by petroleum contamination (not otherwise regulated under CERCLA), and even mine-related sites. Combined with improved financial incentives and increased liability protection under state Brownfield legislation, an entire market has emerged.

An important yet less publicized element is that the legislation *expressly* authorizes the purchase of environmental insurance with federal grant monies. In this manner, federal legislators have specifically confirmed the use and value of environmental insurance as a critical tool in Brownfield projects.

Q: What are the substantive provisions of the new legislation?

A: The key elements of the legislation are certain exemptions from and defenses to CERCLA liability, and liability clarification and financial incentives for Brownfield sites.

- Title I - Amendments to the CERCLA liability scheme for certain activities and small businesses include:
 - Conditional exemptions for generators of small quantities of hazardous substances regardless of the size of the generator, and generators of municipal solid waste for specified small businesses and non-profit organizations; and
 - Codification of specified conditional defenses to CERCLA liability for innocent landowners, contiguous property owners, and bona fide prospective purchasers of environmentally impaired properties
- Title II - Brownfield revitalization and environmental restoration for Local and State governments and Indian tribes, including:
 - Codifying and expanding the meaning of the term “brownfield site”
 - \$250 million per year (through '06) in funding measures for key programs
 - Liability clarification and limited liability relief at certain brownfield sites
 - EPA’s funding and reduced oversight of State Voluntary Cleanup programs (VCP’s)

Q: Why are Brownfield properties important?

A: In the United States, real property is a valuable asset, particularly in the current economy. While most real estate is put to productive use, many Brownfield sites remain unused or under-utilized because of real or perceived contamination and its associated liabilities. The main purpose of federal and state Brownfields programs is to clean up and reuse Brownfields to produce environmental, public health, and economic gains.

Q: What are the environmental concerns associated with Brownfields?

A: There are generally two major concerns associated with a Brownfield site. First, under CERCLA, past, current, and future owners of a contaminated property may be held liable and responsible for the cost to clean up the site. For owners of surplus property not already in some regulatory-driven cleanup program, this is problematic. A potential buyer's due diligence may discover conditions that impose a reporting obligation on the owner and result in enormous liabilities and resulting costs. CERCLA liability is also a concern for potential buyers because their strategy may be to purchase a Brownfield inexpensively, clean up the property, redevelop the location, and ultimately sell the property for a profit.

For this reason, the cost of any cleanup is a crucial variable in the decisions to either sell or invest. These costs have a major impact on the price sellers can achieve for surplus properties, and on ultimate profitability for real estate developers and investors. When a redeveloper becomes the seller of the property, they often must provide the prospective buyer with indemnification against future liability from past contamination. Usually, these issues are critical during real estate transactions involving Brownfields.

The second concern is third party toxic tort liability claims alleging bodily injury, property damage, or natural resource damages resulting from ownership or operation of a contaminated site. For the seller, the fear that such a claim could somehow result from a potential buyer's due diligence is enough to keep the site off the market. For developers, third party liability claims are a potentially huge variable cost that can also destroy return on investment. These potential exposures are crucial in real estate transactions involving Brownfields and have, more than once, entirely thwarted a transaction.

Q: Does the environmental insurance market have solutions available that may help facilitate Brownfield Redevelopment?

A: Yes. The environmental insurance industry has several types of insurance products that can assist with the transfer and redevelopment of contaminated property; policies that respond to all phases from the original testing and planning through final reuse or redevelopment and construction. However, the two most often used solutions are generally known as Cleanup Cost Cap (CCC) and Pollution Legal Liability (PLL) policies. A CCC policy acts as a financial tool that allows a company to limit the costs related to the cleanup of known contamination property. A PLL policy is intended to protect the owner/developer from unknown contamination and related liability issues that may arise during the ownership, cleanup, redevelopment, construction, and operation phases of a project.

Q: Why would environmental cleanups exceed original cost estimates?

A: Environmental cleanups have a history of exceeding projected cost estimates. Cost overruns can occur due to several reasons, which include, but are not limited to, the unanticipated failure of the selected remedial technology, the identification of additional contamination, the determination that known contamination is also migrating offsite, changes in environmental cleanup regulations, and underestimation of time for project completion.

Q: How does the CCC Program work?

A: A typical cleanup requires a Remedial Action Plan (RAP) that outlines the delineation of the contamination being remediated, the methods to be used and tasks needed to complete the cleanup, and detailed time and cost estimates for the project. The actual cost detailed in the RAP is a known liability, and therefore must be retained by the insured. The insurance layer provided by the CCC policy responds to cost overruns in excess of the known liability plus a negotiated buffer layer, which acts as a deductible. This buffer layer is often ten percent of the total cleanup cost. A coinsurance feature may also be incorporated into the insurance limit.

In addition, a finite risk or risk financing mechanism can be incorporated into the program to fund for known cleanup costs using discounted, net-present-value dollars. Also known as Blended Finite Risk, these products are commonly used in the evolving market for guaranteed fixed price remediation and liability buy-out structures, for Brownfield and other cleanup projects. Blended Finite Risk programs incorporating CCC are an excellent alternative to purchase price discounts, escrow arrangements, and other financial hurdles in Brownfield transactions.

Q: What are the benefits of a CCC?

A: A CCC can eliminate future uncertainties associated with cost overruns from cleanups of contaminated properties. This benefits property owners who choose to clean up a site prior to transfer by allowing them to achieve cost certainty. This benefits real estate investors and developers by allowing them to develop firm cost estimates for cleanups, and in turn, more accurately evaluate total investment costs and ultimately their expected return on investment.

Q: Can a CCC cover multiple locations?

A: Yes. Coverage can be crafted for a single site or aggregate programs can be structured for multiple sites under one policy form.

Q: What limits of liability are available in the environmental insurance marketplace?

A: Marsh has structured CCC programs with \$800 million in limits for a single site, and over \$800 million in limits for multiple site cleanups. Most of the major environmental insurers offer limits of \$25 million to over \$100 million on a single policy. Even with recent insurance market hardening, capacity of over \$500 million remains available.

Q: What is the maximum policy term available in the marketplace?

A: The maximum policy term (duration) available in the marketplace is generally 30 years. However, these policies are generally purchased with five to ten year term, usually to coincide with the performance of the RAP. Long term operations and maintenance (O&M) costs can be included on large projects and Blended Finite Risk programs.

Q: How much do these programs generally cost?

A: The typical cost of CCC is between eight – twelve percent of the estimated cleanup cost for a limit of insurance equal to the estimated cleanup cost. The program usually includes a ten percent buffer (deductible). Coinsurance features as part of the limit, higher or lower (percentage) buffer layers, and the nature of the cleanup project all serve to increase or decrease premiums.

Q: What types of coverages are available in a PLL?

A: The primary intent of a PLL is to pay for first party (onsite) environmental cleanup costs that result from pollution conditions that are unknown and unexpected at the beginning of a project, and for related claims alleging third party bodily injury & property damage and defense expenses. A PLL policy can also incorporate coverage for business interruption and extra expenses, project delays, and the transportation and disposal of waste.

Q: What are the benefits of a PLL?

A: PLL can often help sellers achieve a higher sales price by providing buyers with a strong alternative to indemnification. Buyers can use PLL to backstop a seller's indemnification. During a redevelopment project, a PLL policy can protect against unknown pre-existing contamination that is discovered after project commencement, and any related third party claims. These unanticipated costs can destroy developer's and investor's returns. After a remediation project is complete, a PLL can protect a current and future property owner from future environmental liabilities resulting from changes in environmental regulations and regulatory reopener provisions. In this manner, PLL can often help facilitate the closing of a real estate transaction by acting as an environmental warranty for a prospective purchaser.

Q: Can a PLL cover multiple locations?

A: Yes. Aggregate coverage can be crafted for a single site or multiple sites under one policy form.

Q: What limits are available in the environmental insurance marketplace?

A: Marsh has structured PLL programs with limits as high as \$800,000,000 per occurrence or \$800,000,000 aggregate. Individual insurers offer PLL limits ranging from \$25,000,000 to over \$100,000,000. Even in today's changing insurance markets, limits in excess of \$500,000,000 can be achieved for large, complex transactions.

Q: How much do these programs generally cost?

A: The cost for a PLL program varies based upon the number of covered locations, the nature of the potential exposures, the availability and reliability of technical environmental data, as well as the limits, deductibles, and length of policy term. However, premiums have decreased significantly over the past ten years, even as coverage has expanded dramatically. Even in the tightened insurance markets today, PLL remains very affordable, particularly as a percentage of most transaction amounts.

Q: Can a CCC and a PLL program be combined?

A: Yes, it is quite common to combine CCC and PLL programs into one manuscripted coverage form to provide coverage for the known and unknown issues associated with a single site or multiple sites. When integrated into a Blended Finite Risk program, CCC and PLL can form a solid wall of environmental protection, while shifting time, investment, and underwriting risk to a creditworthy third party insurer.

Q: Who are the major insurance carriers?

A: AIG Environmental, XL Environmental, Chubb Financial Solutions, Zurich North America, and ACE Insurance Group. Other carriers include Liberty International, Arch Capital, and Gulf Insurance.

Q: What other services does Marsh provide for Brownfield projects?

A: Marsh has developed strategic and financial environmental risk consulting services specifically for complex transactions such as Brownfields. These include:

- Environmental Risk Identification & Quantification – helps clients understand the nature and magnitude of environmental cleanup and tort liability costs, using decision science, statistical modeling, and other technical competencies. Can help buyers or sellers determine defensible estimates for transaction negotiation.
- Insurance Asset Recovery – helps clients locate and capture a source of capital that exists in old CGL and Excess Liability policies to pay for past, present, and future environmental cleanup costs.
- Program Management – helps clients successfully integrate and manage the scientific, legal, regulatory, and financial aspects of Brownfield projects to achieve their objectives.
- Recognizing that successful Brownfield projects require the delivery and integration of a wide array of highly specialized disciplines, Marsh has developed relationships with industry leaders in:

- Real estate analysis and advisory services
- Environmental consulting and remediation
- Debt financing and equity investment
- Environmental law
- Developers and end-users
- Guaranteed fixed-price remediation and liability buy-out specialists

Brownfield use can be complicated. State and local government programs vary. Issues, such as environmental remediation, liability protection, financial incentives, and repositioning the site are interrelated.

Federal and state legislation in conjunction with private sector innovations, capital, and experience have helped fuel a vibrant, evolving market for Brownfields. Environmental insurance and risk consulting will continue to play an important role in this evolution.

The information contained in this document provides only a general overview of subjects covered, is not intended to be taken as advice regarding any individual situation and should not be relied upon as such. Insureds should consult their insurance and legal advisors regarding specific coverage issues.

Statements concerning legal matters should be understood to be general observations based solely on our experience as insurance brokers and risk consultants and should not be relied upon as legal advice, which we are not authorized to provide. All such matters should be reviewed with the client's own qualified legal advisors in these areas.

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