Connecticut Law Tribune

April 9, 2012

An ALM Publication

LAND USE & ENVIRONMENTAL LAW

Redeveloping Brownfields: The Need for Risk Transfer Strategies

Consulting contracts and insurance policies can help control costs

By ANDREW N. DAVIS and AARON D. LEVY

Recently, state agencies, environmental consultants, law firms and others have published descriptions of the provisions and mechanics of Section 17 of Public Act 11-141, Connecticut's Brownfield Remediation and Revitalization Program (the "Brownfield Program"), whose goal is to incentivize the private sector to develop brownfield sites in Connecticut. This article provides some strategic thoughts about how property owners and developers can best take economic advantage of the program and points out the need, given the program's limitations, to do so in coordination with other innovative environmental risk transfer strategies, such as guaranteed fixed price remediation (GFPR) contracts and/or environmental insurance.

In general, the Brownfield Program provides innocent land owners (among others who apply for and are accepted into the program) with certain liability protections related to the development of contaminated and underutilized properties. While the improved liability protections available through this new program are important, with proper scrutiny it becomes clear that the Brownfield Program, which can only accept 32 applicants a year, does not fully protect innocent purchasers/developers and "box-in" all of the potential risk associated with the ownership/development of a contaminated site.

The Brownfield Program does provide certain benefits in that successful applicants: (1) have no obligation to investigate/remediate off-site impacts related to known historic on-site conditions, and (2) are afforded liability protection under state law from certain (cleanup-related) claims by the state and/or third parties related to known historic releases on or from the site.

Andrew N. Davis

Aaron D. Levy

However, participants in the Brownfield Program still are responsible and liable for the investigation and remediation of on-site conditions. Furthermore, the liability protections afforded by the program do not protect against certain instances — for example, third-party bodily injury or property damage claims (i.e., "toxic tort" claims), previously unknown contamination that resulted from a release that occurred before the date the applicant was accepted into the program, or claims pursuant to federal laws (e.g., for federal natural resource damages). Potential applicants also should be aware that eligibility into the Brownfield Program is limited to sites that are not, among other things, subject to an enforcement action, listed on the national priorities list or the state's Superfund Priority list, or subject to corrective action under the Resource Conservation and Recovery Act (RCRA).

Thus, although there are advantages for development of some state brownfield projects, many potentially valuable brownfield sites do not meet the Brownfield Program's participant and site eligibility criteria, requiring their environmental risks to be managed outside of a formal program.

GFPR Contracts

Anyone considering acquiring or developing a brownfield site should evaluate not only applicable state/federal programs (including the Brownfield Program), but also market-based environmental risk transfer strategies, including GFPR contracts offered by certain sophisticated environmental consulting firms and/or environmental insurance. Through a combination of applicable regulatory programs and available market-based risk transfer mechanisms, savvy developers will be able to structure deals to box-in all (or nearly all) environmental risks associated with a contaminated property.

For example, in recent years, certain en-

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vironmental consulting companies have evolved from solely conducting remediation on a "time and materials" basis to contractually assuming certain environmental liabilities through a GFPR contract. Not only will these companies perform the environmental remediation necessary to clean up the property, but they will do so for a pre-defined fixed price, assessing and quantifying a company's environmental liabilities and contractually assuming the remediation and regulatory obligations (including, in certain instances, entering into a consent order or voluntary cleanup program with the EPA or relevant state environmental agency). Accordingly, it may be possible contractually to box-in the risk associated with potential remediation cost overruns (which are common when the investigation and remediation is conducted on a time and materials basis) by entering into a GFPR contract (or "liability transfer").

Essentially, a GFPR contract allows a developer to contractually transfer to an environmental consulting firm the obligation to remediate the site for a fixed fee. The consultant estimates the total cost of the remediation (e.g., by utilizing likely best and worst case scenarios through "Decision Tree" and "Monte Carlo" or other analyses) and present values the total estimated cost. Accordingly, a GFPR contract can affix a single fixed cost to the resolution of a developer's environmental remedial liabilities and negate (or mitigate) the risk of potential cost overruns. Notably, a GFPR contract could protect even those developers that are accepted into the Brownfield Program from potential cost overruns related to on-site remedial obligations. (Note also that although the market for such products is limited at this time, a tailored "cost cap"/stop-loss remediation environmental insurance program may be available on a case-by-case basis to wrap around the consulting firm's obligation pursuant to a GFPR contract.)

A properly structured GFPR contract can be designed to align the interests of all the parties involved, for example, by incentivizing the consultant to complete the remediation under budget and on time (e.g., by awarding a "completion/success bonus") and disincentivizing the consultant from reaching the insurance layer, if one exists (e.g., by requiring the consultant to charge its labor at a reduced rate and/or limiting or prohibiting mark-ups on subcontractors once the insurance layer is reached, and/or requiring the consultant be responsible for a co-insurance allocation). As a further safeguard, a GFPR contract may be structured to require the environmental consultant to complete the remediation "at cost" in the event that the budget structure is exceeded or, where environmental insurance may have been available, any/all available insurance is exhausted.

Pollution Liability Insurance

While a GFPR contract can mitigate the risk of potential cost overruns associated with cleanup obligations, it typically does not protect against the risk of third-party toxic tort claims. If properly structured, pollution liability environmental insurance policies (which are broadly available in the market, unlike the remedial environmental insurance products mentioned above) can be written to cover a broad spectrum of potential environmental liability exposures beyond remediation cost overruns. These can include traditional pollution legal liability coverages (some or all of which an environmental consultant/liability buyout firm likely would not take responsibility for by contract) such as claims for third-party bodily injury and property damage; natural resource damages; liability associated with transportation and disposal of hazardous wastes/substances; project delays and business interruption; loss of collateral value; contract liability; and legal defense costs.

It is also important to note that such pollution liability-based environmental insurance policies can provide limited cleanup cost coverage, but only for remediation of pollution conditions not previously identified after appropriate due diligence (i.e., "unknown" pollution conditions) or for "known" pollution conditions, after "no further action" is achieved to protect against future regulatory reopeners/changes in cleanup standards.

Note that an environmental insurance policy is, in its essence, a contract and needs to be negotiated and tailored (manuscripted) to the specifics of the situation and the underlying cleanup/environmental risks. For example, a manuscripted environmental insurance program could mitigate the financial risk associated with potential bodily injury and property damage claims by nearby property owners and/or federal natural resource damage claims from which, as noted above, the Brownfield Program would not protect participants. In general, off-the-shelf, template or specimen environmental insurance policies are not appropriate for these types of transactions (and can be greatly enhanced beyond specimen language).

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Ultimately, while state and federal programs, including Connecticut's Brownfield Program, provide some valuable incentives and protections for brownfield developers, they rarely resolve the full suite of potential liabilities associated with contaminated sites. Similarly, in light of the eligibility requirements associated with the Brownfield Program (and similar state/federal programs), many underutilized (and potentially valuable) sites may not qualify for acceptance into the program. However, through innovative environmental risk transfer mechanisms and the strategic use of environmental insurance, a sophisticated developer may utilize market-based mechanisms to box-in all (or most) environmental risks associated with a brownfield site, whether or not it qualifies for the Brownfield Program.•

Andrew N. Davis, Ph.D., is a partner and Aaron D. Levy is an associate in the Real Estate, Environmental and Land Use Practice Group at Shipman & Goodwin LLP in Hartford. They have been involved in several high-profile real estate, corporate and energy deals in Connecticut and nationally involving contaminated property, utilizing environmental insurance and other risk transfer mechanisms to creatively manage environmental risks. Andrew can be reached at adavis@goodwin.com; Aaron can be reached at alevy@goodwin.com.

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