

## **The Urban Brownfield**

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For nearly three decades owners of brownfields properties have faced expanding adversities, including government regulations, broadening environmental liabilities and increasing litigation, all of which have negatively impacted, and in some cases completely wiped out, the economic value of their property.

While responsible parties and brownfields properties have been identified, there has been limited success to stimulate clean up activities stalling one of societies' greatest interests – the transformation of urban and industrial areas into revitalized economically viable real estate. This is due in large part to the low economic value of these properties and the high risk a developer is required to accept in commencing the cleanup efforts necessary to redevelop a brownfield property.

Over the past few years, after recognizing that these regulations were being interpreted in ways that actually discouraged owners to cleanup and more importantly to redevelop brownfields sites government bodies have initiated change. The states and the federal government have enacted new legislation affording owners, buyers, and developers of contaminated real estate protections from some of these environmental liabilities and in some cases economic incentives for clean-up activities. Environmental regulators can now take into account restrictions on future land uses when setting property specific cleanup criteria. The consistency of agendas among federal and state environmental

agencies has also helped to pave the way for a more efficient and successful redevelopment process.

At the federal level, the US Environmental Protection Agency has shifted its classification criteria to a more potential risk and land use-based approach for Brownfields properties. One telling action is the de-listing of tens of thousands of sites from the CERCLA database in an effort to remove the historical environmental stigma associated with these types of properties.

Recently, in a concerted effort to further stimulate the redevelopment of urban and industrial areas, the Congress and Senate enacted the Small Business Liability Relief and Brownfields Revitalization Act (“LRA”) revision to superfund liability. This act potentially benefits any party who owns contaminated property, wants to purchase contaminated property, or is potentially liable for remediation of non-owned contaminated property. This act also provides State’s with funding for environmental assessments, remediation, and the implementation of Brownfields programs in support of state established cleanup programs.

While at the state level, some regulatory agencies have implemented initiatives encouraging participation in voluntary cleanup programs and have shifted regulatory oversight of brownfield sites to Licensed Environmental Professionals (LEPs). Furthermore, states have initiated investment incentives in the form of tax benefits and low interest loans to Brownfields developers. Numerous state cleanup funds have been established to further assist with the expense of remediation. Additionally, state and local agencies have removed some of the time hurdles and project approval impediments in a further effort to expedite the start of redevelopment efforts.

This new climate combined with the shortage of developable real estate has begun to fuel increased demand for these sites. Investment opportunities abound for developers willing to engage in Brownfields projects, especially when one considers that these sites are often

centered in urban markets with existing infrastructure and positive demographics that help attract and retain class A tenants.

Traditionally, owners of Brownfield properties have had few attractive means of divestiture. The new Brownfields Legislation has given owners the opportunity not only to sell these properties but also to participate in the redevelopment that can provide an additional source of capital to fund the cost associated with remediation.

Often a Brownfields developer can minimize cleanup costs through the use of deed restrictions and implementation of institutional controls negotiated with the overseeing regulatory authority when a remediation plan is being developed. “We structure our redevelopment plans and property use strategies based upon the most economically viable remediation plan”, says Joe Cotter, President of National Resources, a national Brownfields property developer. For example, a developer of a mixed-use property may agree to implement deed restrictions in exchange for less stringent cleanup criteria. Specifically, areas to be used for housing may require a higher cleanup standard, while a retail/commercial use may simply require capping the contamination in place, a cost effective solution. In the past, bifurcating the property use in this manner was not possible as cleanup standards were always unilateral based on the permitted property with the highest or most “pristine” cleanup standards.

While this regulatory evolution and creative land use planning have removed numerous obstacles, significant long-term environmental liabilities remain. Typically, Brownfields properties were used by various types of manufacturing and industrial operations resulting in complex on and off site soil and groundwater contamination. It is essential to evaluate the historical and future liability exposure for not only cleanup costs, but also potential third party bodily injury and property damage claims.

The liability associated with owning environmentally impacted property lasts far into the future creating a legacy “tail” that is very difficult to manage. Even after a Brownfields

redevelopment project has been completed, source area contamination has been remediated and regulatory closure has been achieved, legacy liabilities remain. Corporations must diligently manage on-going risks such as plume migration and the potential for third-party liability claims. The insurance industry has responded to this concern and need of owners and developers by developing environmental insurance products that provide coverage for these environmental liabilities.

Environmental insurance serves as a viable alternative and/or enhancement to traditional risk shifting tools attorneys and consultants have used to manage these environmental liabilities. These new policies can reduce cleanup cost uncertainty and the need for indemnification agreements, price reductions, or funding of escrow accounts allowing brownfields redevelopment to proceed.

Pollution legal liability is the most flexible of these policies and is specifically designed for real estate transactions and brownfields projects. The policy can provide coverage for third party bodily injury and property damage claims, on-site and off-site cleanup costs for historical and future contamination, as well as legal defense expenses. There are many endorsements available to broaden these policies including but not limited to business interruption, diminution in adjacent property value, contractual liability, mold, asbestos, and lead based paint.

In a recent brownfields project involving a 95-acre property with numerous buildings totaling 1.4 million square foot of vacant manufacturing space, the developer utilized environmental insurance. Years of solvent disposal resulted in the formation of a 300-acre plume that was both on and off-site. The plume was moving one foot per day and had contaminated several local municipal drinking water supplies.

As part of the purchase and sale agreement the seller provided an environmental indemnification agreement to the developer that covered remediation expenses as well as third-party liability claims for known contamination. However, given the magnitude of

the plume, and an estimated \$30,000,000 remediation cost the developer could not attract interested investors or lenders. Through the implementation of a pollution legal liability policy providing coverage excess of the indemnification agreement the developer was successful in funding the project. The owner was a publicly traded company, however its industry was in decline raising concerns about its long-term financial stability. The policy alleviated the investor and lender concerns regarding owner solvency as it backstopped the indemnification agreement.

The owner sold an idle property that it could not put to productive use and the developer completed the project that today, includes a high tech office complex. The insurance aligned all parties involved in the transaction as it effectively covered the long-term environmental liabilities, a risk that, in the past, would have remain unmanaged.

### **Pollution Legal Liability Policy Detail**

Liability Limit: \$50,000,000

Self-Insured Retention: \$150,000

Policy Period: 10 Years

#### **Coverage Provided:**

On-site cleanup of historical conditions (excess of indemnification)

On-site cleanup of new conditions

Off-site cleanup of historical conditions (excess of indemnification)

Off-site cleanup of new conditions

Third-party claims for bodily injury and property damage (excess of indemnification)

Diminution of adjacent property value

Business interruption-actual loss of rental income

Additional insureds – lender and investors

Cost-cap and finite risk policies are designed to address the risks that property owners and developers face during a remediation project. These policies minimize the financial uncertainties, the technical and regulatory challenges and balance sheet issues associated with these types of brownfields projects. The policy can be designed to cover a variety of situations that may include approved remedial plans as well as plans in progress. Coverage can be included for known and unknown contamination ensuring that cost over runs don't affect the projects financial success.

For example, in a transaction involving a 35-acre property with dilapidated structures that contained large quantities of asbestos and lead-based paint. Located in a former industrial area that local land use officials have targeted for mixed-use redevelopment. Soil and groundwater contamination existed from historical manufacturing operations that included heavy metals and arsenic. State licensed professionals through sub surface investigations fully characterized the contamination and delineated the source area and plume concluding that all contamination was contained on-site.

Through a well crafted acquisition agreement and properly structured finite risk cost cap policy the developer was able to acquire the property removing remediation expense uncertainty while the owner was able to sell the property removing environmental balance sheet liabilities.

In the negotiation, the developer agreed to provide a finite risk cost cap policy providing cost over-run protections for both parties. The insurance policy also alleviated the owners concern of funding the expected cleanup costs to the developer with no guarantee that the funds would be protected or that the remediation would be completed. The policy was funded by a one-time payment to a triple A rated Carrier that combined the cleanup cost estimate and cost over-run protection in one seamless policy. The policy provided ground up coverage with no deductible, buffer layers or co-insurance requirements.

The cleanup was estimated at \$5.7 million that also included building demolition and the removal of the asbestos and lead-based paint. The Voluntary Cleanup Agreement (VCA) was structured to take into account the objectives of the redevelopment, granting of deed restrictions and the requirements of state and local authorities. The insurance carrier agreed to provide a policy with a \$12 million limit and working with a third-party environmental contractor took financial responsibility for the remediation up to the policy limit and the administrative burden of regulatory compliance as set forth in the VCA. This approach enabled the developer to establish a viable project budget, whereas remediating to “pristine” cleanup standards with no protection would have been risk prohibitive.

Owners and developers of brownfields properties recognize their on-going liabilities and in order to manage them are utilizing environmental insurance to protect them going forward. An environmental insurance policy, drafted to address the specific exposures of a property, affords them the most complete protection from these liabilities going forward. Environmental insurance policies can be used to: manage the uncertainty of cleanup costs; transfer first party and third party liabilities associated with a property; minimize the risks related to changing regulatory and cleanup standards. Properly structured and implemented environmental insurance can help meet the objectives of the developer, the property owner and the lender aligning their interests even further, thereby helping to ensure the success of a sale and/or redevelopment effort.