

Environmental Insurance

Topic: Environmental Insurance

Description of the issue:

If a property is not remediated to an unrestricted use, then institutional and/or engineering controls must be implemented as part of the cleanup. The obligation to maintain, monitor and report to the Department on the protectiveness of the institutional or engineering control continues with each new property owner, lessee or operator. This obligation requires time and money, as well as the knowledge of the obligation. In some cases, it is a developer that remediates and redevelops a property by establishing an institutional or engineering control, the responsibility to comply with the maintenance, monitoring and reporting requirements is passed on to homeowner or, a homeowners association or a condo association. For example, the developer may establish a limited liability corporation (LLC) to develop the property, and then dissolve the LLC after the property is developed and sold. Homeowners, homeowner associations and condo associations are not necessarily equipped with the requisite money or environmental knowledge to comply with the long term requirements associated with the controls (N.J.A.C. 7:26E-8.)

Another issue concerns properties (either residential or industrial) that are transferred to new property owners multiple times and/or are rezoned/redeveloped for different uses. In these cases, the responsibility for long term monitoring, maintenance and reporting may get lost. For example, the property may initially be developed for industrial use with an engineering control. Over the years, the market changes and the property use is changed to residential. There needs to be a mechanism to ensure that subsequent purchasers know that they are responsible for the requirements of N.J.A.C. 7:26E-8 and what these requirements entail.

DEP's Current Authority:

The Brownfield and Contaminated Site Remediation Act at N.J.S.A. 58:10B-12, allows for a remedy of a contaminated site at which a responsible entity leaves contamination on-site, regardless of whether the property is going to be used for residential or industrial use, as long as the implementation of the institutional and/or engineering control at that site will result in the protection of public health, safety and the environment. Further, N.J.S.A. 58:10B-13 requires that the owner or lessee of any property for which there is an institutional and/or engineering control as part of the remedy, to maintain the institutional or engineering controls. The Department's regulations known as the Technical Requirements for Site Remediation, N.J.A.C. 7:26E, require that the owner or lessee monitor the protectiveness of the institutional and/or engineering control and to report to the Department on its findings on a two year cycle.

Background:

In 2003, the Department adopted a new subchapter to the Technical Requirements for Site Remediation at N.J.A.C. 7:26E-8 that describes the Department's requirements for monitoring the protectiveness of institutional and engineering controls and reporting the findings to the Department. These requirements include that each owner, lessee or operator of a property that is subject to an institutional and engineering control conduct periodic inspections of the site to ensure that the department approved controls remain

Environmental Insurance

protective at the site regardless of the property use. . This obligation “runs with the property” therefore, each subsequent owner, lessee or operator of the property bears this responsibility.

The Department presented options to the stakeholders involving the use of environmental insurance products, for which a market is developing, to address the issue of long term maintenance, monitoring and reporting as well as addressing future protectiveness of a remedy. Since environmental insurance is a tool to allow transactions to occur when environmental conditions exist, there may be a use for an insurance policy when sites are transferred that have been remediated using an engineering or institutional control. These restricted-use remedies have continuing obligations pursuant to the Technical Requirements for Site Remediation, such as monitoring, maintenance and biennial certifications (which attests that the remedy is still protective.) The monitoring, maintenance and biennial certification requirements of engineering and institutional controls are the obligation of 1) a person with a legal obligation to conduct the remediation, and 2) each owner, lessee and operator of a property, limited to that period of that person’s ownership. An insurance policy may assist in guaranteeing that there is always a fund to provide the resources to perform the monitoring and maintenance. In addition, the insurance policy may be able to provide the additional funding in the event the biennial certification identifies that a remedy is no longer protective and the site requires further remediation. Two types of products were discussed: those that insure that money is available to comply with the monitoring, maintenance and reporting requirements of N.J.A.C. 7:26E-8, and those that insure against harm or damage to public health and the environment from the failure of an engineering control.

The first insurance product would be for all limited-restricted or restricted use remedies using either institutional or engineering controls on the property. The product would insure that there was a funding source for the proper monitoring, maintenance and reporting required under existing regulation and would cover any increased costs associated with a change in monitoring or reporting requirements. It may not be necessary for the insurance to be obtained by the remediating party, but the requirement for the insurance would be triggered once the property is transferred. This payment for an insurance policy may create an incentive for a property owner to implement a permanent remedy and thereby avoid the future requirement for insurance and potentially increase the value of the property. Legislation could mandate that all properties with institutional/engineering controls be covered by this insurance and no property could be transferred without having this insurance. The cost of the insurance could be borne either by the seller or the purchaser, and would become part of the negotiations of the sale of the property. Requiring this insurance would raise the awareness of the nature of the institutional/engineering controls on a property and assure that knowledge of controls and associated requirements is transferred with the property to the new owner.

The second product, possibly an insurance fund or a trust, would be created to fund additional remediation required as a result of the adoption of more stringent remediation standards, or resulting from the catastrophic engineering failure of a remedy. Legislation could require any remediating or responsible party that does not implement a permanent

Environmental Insurance

remedy to pay into the fund to cover the above stated additional potential remediation needs. The amount a party must contribute to this fund could be based on the level of remediation achieved by the clean up, the levels and types of contamination left behind, or the potential risks posed by the site should the institutional/engineering controls fail.

Those remediating parties that perform an unrestricted use cleanup would not be required to contribute to this fund and their liability would end with the No Further Action Letter/Covenant Not To Sue (NFA). If the remediating party is protected from the liability of cases being re-opened (even if remediation standards change by an order of magnitude), it may drive more remediating parties to implement a permanent remedy by ensuring finality. Those remediating parties that do not clean up a site to an unrestricted use standard would be required to contribute to the above fund and remain liable for ongoing monitoring and maintenance, biennial certifications, remedy failure and re-opened cases due to a change in standards by an order of magnitude. The fund could be used to correct the remedy failures or corrective actions for those cases where the Department is unable to get the responsible party to rectify the problem.

Stakeholder Comments:

The regulated community had many concerns about environmental insurance as a solution to the issue of ensuring long-term maintenance, monitoring and reporting, and implementing future remediation requirements. It has been the experience of some stakeholders that it is often difficult to collect from insurance companies and that the cost of insurance is prohibitively expensive. In addition, insurance policies are limited in nature; generally written for a term no longer than 10 years with no guarantee of renewal; and cover very specific tasks. Monitoring and maintenance requirements are often for a period much longer than 10 years. Another concern raised was that a policy for ensuring the maintenance of an engineering control might be viewed as insuring an “illegal” activity. In other words, if an engineering control was not properly maintained, it would be in violation of statute and regulation, and the insurance company would therefore be paying a claim that is based on a violation of state requirements. Lastly, stakeholders felt that since a redeveloper has to secure the funding to address other areas of maintenance at a site, the maintenance of institutional controls could be included in the overall building maintenance. If additional costs were required for this type of maintenance, it would ultimately be passed on to the end user.

Stakeholders identified issues with affordability and effectiveness of the existing environmental insurance products and felt that no existing insurance product served the intended purpose of the Department and suggested that the Legislature create a public “pool” of money, analogous to the uninsured drivers fund, to cover the costs in instances where the responsible entity fails. To guarantee the monitoring and maintenance of institution and engineering controls, legislation could impose a transfer tax on real estate transactions in order to fund this initiative. The regulated community felt that the use of this type of fund would ensure that money exists to comply with the maintenance, monitoring and reporting requirements in instances where a responsible entity fails to do so, without forcing developers who did not cause the contamination to use their funds to

Environmental Insurance

guarantee the long-term protectiveness of the remedy. All agreed that the imposition of another tax could be an impediment to passing the legislation required for this type of fund.

Finally, the regulated and environmental community suggested that the Department create a permit program for sites that have an institutional or engineering control. In this model, the Department would require a remediating party that chooses to remediate a site using a non-permanent remedy (thus requiring an institutional and/or engineering control) to obtain a permit from the Department which contains the maintenance, monitoring and reporting requirements for that site. This permit would be transferable to subsequent property owners. The permit program is a more transparent system than the current requirements for institutional and engineering controls that automatically subjects subsequent owners, operators and tenants to the monitoring, maintenance and reporting requirements of the Technical Regulations for Site Remediation. The issue of environmental insurance is closely linked to the White Paper addressing Engineering and Institutional Controls and stakeholders suggested addressing the two issues together.

Other States: Environmental insurance is a useful tool in managing the risk associated with the remediation of a contaminated site. There are several types of environmental insurance policies currently available. These products are often used in the conveyance of a brownfield site to limit a buyer's financial liability associated with 1) potential escalating costs of remediating known contamination (referred to as "Cost Cap Insurance") and 2) additional remediation costs for unknown contamination (referred to as "Pollution Legal Liability Insurance"). During the negotiations of the sale, the buyer and seller allocate contractually the responsibility for any remaining remediation activities or costs. Often times these costs are not known at the time of the sale and the contract will include the buyer or seller purchasing a Cost Cap insurance policy to ensure that if the remediation costs exceed an anticipated amount, there will be funds to cover those added costs. In addition, the buyer may want to protect itself from having to incur costs for contamination not known at the time of purchase by obtaining a Pollution Legal Liability policy. A third type of insurance policy is the Finite/Blended Risk policy that transfers the environmental financial liabilities to an insurance carrier. The responsible party pays the insurance carrier the present value of the projected cost of the remaining remediation plus an additional risk premium. In return, the insurer takes on the financial responsibility of the remediation. This type of policy can include aspects of the Cost Cap Policy (for known contamination) and the Pollution Legal Liability policy (for unknown contamination.)

The New Jersey Environmental Risk Management Fund was established to deal with the special problems of brownfields. The effort was undertaken by an alliance of municipalities to provide coverage for a range of environmental liability exposures and related costs in urban redevelopment. In New Jersey, 199 small cities have joined together to create the Environmental Joint Insurance Fund (EJIF) to protect themselves with coverage from a range of environmental liability exposures and related costs, some of which contribute to facilitation of urban redevelopment. EJIF covers a population of

Environmental Insurance

about 2 million people and includes municipalities with as many as 60,000 residents. The current program covers four major classes of risk:

1. Environmental liabilities related to current municipal operations;
2. Liabilities related to hazardous materials accident responses that damage potable drinking systems and runoffs to stormwater systems;
3. Site-specific coverage for illegal dumping by unknown parties on municipal property, including costs for emergency cleanups, if needed, municipal contributions to abandoned waste disposal facilities that have been classified as Superfund sites; and
4. Public officials' liability for actions excluded from standard municipal liability coverage.

Below is a summary other state environmental insurance programs. Most of the programs address subsidies for parties that want to obtain environmental insurance or standardize insurance policies obtained through the state by working with a single carrier.

Massachusetts: The Commonwealth enacted broad legislation to promote the environmental cleanup and redevelopment of Brownfields sites across the state. The Brownfield Redevelopment Access to Capital Program (BRAC Program) was created as part of that legislation. The BRAC Program makes high quality, state-subsidized environmental insurance available to most parties who wish to purchase, clean up and develop Brownfields sites anywhere in the Commonwealth. Often, lenders who finance eligible projects can also obtain subsidized protection through the program. The primary benefit of the BRAC Program is that the Commonwealth of Massachusetts subsidizes a substantial portion of the cost of this insurance for parties/sites that meet eligibility requirements.

Wisconsin: There are two insurance programs in Wisconsin: the Voluntary Party Liability Exemption Insurance Program and the Wisconsin Brownfield Insurance Program.

If a voluntary party wants to obtain Wisconsin's equivalent of an NFA for a site relying on natural attenuation before the ground water standards are met, then they are required to obtain environmental insurance through a state program to cover the cleanup cost of the site should the natural attenuation remedy fail. If the voluntary party chooses not to pay the insurance fee, then they must continue to monitor the contamination at the site, wait until the ground water standard is met and then apply for the NFA. Wisconsin has entered into a master insurance policy to provide security for the State when issuing an NFA for sites relying on natural attenuation. If the site needs to be re-opened due to the failure of natural attenuation, the insurance will cover certain State cleanup and investigation costs.

The Wisconsin Brownfields Insurance Program (WBIP) is an optional environmental insurance program for Wisconsin developers, businesses, and local governments. The program is designed to help protect against unknown environmental liability and ensure

Environmental Insurance

that redevelopment of brownfields properties is a profitable venture, particularly for medium-to-small sized brownfield projects. The WBIP is offered as an option for medium-to-small sized brownfield projects that were not being served by the traditional insurance market.

The WBIP standard policy provides coverage for the following:

- investigation and cleanup of previously unknown contamination at, or emanating from the insured location;
- investigation and cleanup of contamination if remedial action was completed and the site was closed (re-opened coverage);
- coverage for third-party claims (bodily injury, property damage and/or cleanup costs) caused by contamination at, or emanating from, the insured location;
- coverage for business interruption for extra expenses and/or lost income caused by unknown contamination at the insured location;
- coverage for pollution claims at, or emanating from, disposal sites where contaminated soil and other materials are disposed of; and
- costs for transportation of cargo, including waste, to or from the insured location.

New York: New York has created a refundable tax credit program to encourage brownfield cleanup and redevelopment. The refundable credits are designed to encourage developers to restore these properties to productive use. There are three components to the refundable brownfields tax credit program, one of which is a tax credit for environmental insurance.