

**State-Sponsored Brownfield Insurance Programs**  
*Face-to-Face with the Environmental Insurance Industry*  
**Colorado Brownfields Conference 2004 October 15, 2004**

**State Program Brownfield Insurance Products**

**A. Pollution Liability (PL) Policies**

**1. Overview:** The risks covered by the policies may be categorized into three main components. The first involves protection against the costs of third party bodily injury and property damage claims. The second consists of protections for the insured against the costs of remediation and related expenses. The third protects against legal defense costs associated with the first two elements.

**2. Coverages that may be provided, depending on the carrier and specific project:**

a. *Third Party Claims*

- Tort liability claims for bodily injury, property damage, property value diminution, and business interruption caused by pollution emanating from the insured's property.
- Onsite bodily injury and property damage caused by pollution.
- Claims due to pollution at or emanating from known or unknown, non-owned disposal sites.
- Release of contamination during transportation.
- Contractual liability due to pollution.
- Natural resource damage caused by pollution.

b. *First Party Onsite Cleanup Costs And Related Expenses*

- Remediation of pollution ordered by a regulator after a cleanup (re-opener coverage).
- Remediation of known pollution originally thought not to require remediation.
- Remediation of previously unknown, pre-existing pollution.
- Remediation of current pollution from ongoing operations.
- Property value diminution, business interruption, and delayed construction costs due to pollution.
- Remediation of pollution emanating from adjacent properties.
- Property damage, property value diminution, and delayed construction due to pollution emanating from adjacent properties.

c. *Legal Defense Costs To Defend Against Third Party Claims*

**B. Cost Cap (CC) Policies**

**1. Overview:** The policies protect against cost overruns that arise in the performance of a remediation plan. The insurer pays the excess costs above a self-insured retention (SIR), typically expressed as a percentage of the estimated cleanup cost. A policy may include a co-insurance provision under which claims that exceed the SIR are shared by the insurer and the insured.

**2. Coverages that may be provided, depending on the carrier and specific project:**

- Costs due to discovery of a greater volume or higher concentrations of contaminants than were noted in the remediation plan.
- Costs due to discovery of contaminants that were not noted in the plan.
- Costs due to regulatory requirement changes during the performance of the remediation plan.
- 'Soft' costs due to a project delay caused by unexpected contamination such as income loss and loan interest incurred during the delay.

**C. Secured Lender (SL) Policies**

**1. Overview:** The policies provide protection for the lender in the event that a borrower defaults and the default is accompanied by a pollution condition (or, in some policies, caused by a pollution condition.) Third party liability coverages also are offered.

**2. Coverages that may be provided, depending on the carrier and specific project:**

- Reimbursement for the lesser of the cleanup costs or the principal loan balance (or, in some policies, for the outstanding principal balance only).
- Cost of third party liability claims for bodily injury, property damage, diminution of property value, and business interruption resulting from contamination.
- Legal defense costs to defend against third party claims.

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## **Massachusetts' Brownfields Redevelopment Access to Capital (BRAC) Program**

### **Overview**

- Enabled by 1998 legislation and implemented in 1999.
- Administered by MassBusiness, a non-governmental economic development organization that reports to the state's Department of Economic Development (DED).
- Offers reduced-cost, pre-negotiated, state-subsidized insurance to those who borrow funds to clean up and redevelop brownfields and to their lenders. Pre-set schedules for PL premium prices are provided.
- *Current status: program active. In process of negotiating biennial insurer contract(s).*

### **Insurance Policies Provided**

- Borrowers can purchase two basic types of coverages:
  1. PL pays for:
    - cleanup costs for on-site, preexisting pollution conditions outside of a Remedial Action Plan area;
    - legal defense, bodily injury/property damage claims related to preexisting on-site pollution conditions;
    - third party claims for cleanup of off-site, pre-existing pollution conditions;
    - legal defense and off-site bodily injury and property damage claims by third parties related to preexisting pollution conditions;
    - business interruption (actual loss, or loss of rental income and extra expense for business interruption related to pollution conditions. (Purchased separately from other PL coverages.)
  2. CC pays for cleanup costs for preexisting known and unknown pollution conditions within a Remedial Action Plan area, which exceed estimated cost of cleanup as determined by the insurer.
- Lenders are protected by a 'mortgagee/insured assignment' endorsement to a borrower's PL policy that converts the policy to the lender should foreclosure be necessary. The provision assures funding for cleanup and protects the lender against bodily injury and property damage claims and legal expenses.

### **Benefits to Users**

- Transfer of environmental risks to insurer.
- State currently provides 25% subsidy of insurance premiums to a maximum of \$25,000 for PL coverages and an additional \$25,000 for CC coverages.
- Current premiums estimated at 30% to 50% below-market rates before subsidy. Cost savings stem from pre-negotiated policies and volume discount offered by insurer.
- Pre-negotiated policy saves users legal expenses and time manuscripting the policy.
- Premium pricing schedules for PL help developers calculate costs to assess the feasibility of a project.
- Insurer provides second opinion of Remedial Action Plans and liability exposures.

### **Eligibility/Participation Requirements**

- Any business or governmental subdivision that obtains loan for brownfield project is eligible for discounted insurance and subsidy (although loan requirement may be waived for local government/community development organizations). A developer not financing a project is eligible for discounted insurance only.
- To participate, borrower submits application, subsidy questionnaire, evidence of financing. No application required for mortgagee endorsement. For Pollution Liability, Phase II assessment required. For Cost Cap, Remedial Action Plan and cost estimates required.

## Insurance Costs

Examples of Current Pollution Liability Premiums Before Subsidy for Five-Year Policy				
Policy Limit	\$10,000 Deductible	\$25,000 Deductible	\$50,000 Deductible	\$100,000 Deductible
\$1,000,000	\$9,642	\$8,386	\$7,715	\$7,128
\$10,000,000	\$44,125	\$41,409	\$37,336	\$33,942

Notes: For Pollution Liability, excluding business interruption. Further discounts apply with CC purchase.

Examples of Current Cost Cap Premiums Before Subsidy					
Estimated Cleanup Cost	Policy Limits	SIR	Premium	SIR	Premium
Up to \$100,000	\$100,000	35%	\$22,778	50%	\$19,361
\$700,001- \$800,000	\$800,000	10%	90% Std Cost	20%	80% Std Cost

Notes: SIR means the Self-Insured Retention (similar to deductible). Std Cost is insurer's Standard Cost. Projects with estimated cleanup costs above \$800,000 receive 5% discount from Standard Cost.

### Program Development Process and Costs

- Enabling legislation envisioned BRAC as loan guarantee program for cleanups, but concept was untenable since few lenders loan just for cleanups. Since insurance was allowed, BRAC modified to be insurance program.
- Policy developed by MassBusiness, Department of Economic Development, attorneys, insurer.
- Cost: MassBusiness and DED staff time. \$250,000 (primarily for attorney fees to review policies).

### Program Administration and Costs

- MassBusiness qualifies applicants, issues subsidy payments, maintains program database, publicizes program, negotiates with insurers every two years.
- Cost to state: \$345,400 per year on fixed-price contract for 2.5 FTEs, marketing, and overhead.

### Program Results, October 1999 - August 17, 2004

Number of projects in program	232
Insurance dollar limits provided	\$879,886,500
Insurance premiums charged	\$10,983,233
Subsidies paid	\$4,655,669
Cleanup costs expended on projects	\$140,157,124
Permanent jobs created or retained by projects	24,235
Total development expenditures - loans and investments leveraged	\$1,829,343,988

### Current Concern about Program

- CC policies for small-scale projects are not cost effectiveness. For \$100,000 expected cleanup, with \$100,000 policy and 35% SIR, the premium without subsidy is ~\$23,000. The insured spends ~\$58,000 above the estimated costs before the policy pays. With a 25% subsidy, the insured would pay ~\$52,000.

## **California's Financial Assurance and Insurance for Redevelopment (FAIR) Program**

### **Overview**

- Bill that established FAIR approved in 2001.
- Program modeled after Massachusetts' BRAC program.
- Effort initiated and led by California Environmental Protection Agency (Cal/EPA).
- Insurance coverages designated to be provided: PL, CC, and SL.
- Funds for subsidies currently unavailable, but legislation authorized subsidies of up to 50% of premiums and up to 80% of SIR for CC policies to a maximum of \$500,000 per project.
- *Current status: insurer provisionally selected. Negotiations in process.*

### **Program Development Process and Costs**

- 1999: Impetus to initiate program came from Cal/EPA when state had budget surplus.
- 2001: Enabling legislation SB 468 passed. Mandated competitive bidding process to select insurer.
- 2002: Consultant assisted in holding stakeholder workshops and preparing Request for Proposals and Qualifications for insurer.
- June 2003: Insurer provisionally selected. Negotiations over policy terms, pricing, program administration began.
- Fall 2003 - Summer 2004: Negotiations suspended.
- August 2004: Negotiations resumed.
- Costs to state: Four years Cal/EPA staff time and substantial state and federal funds spent (primarily for consultant fees).

### **Implementation Delays**

- Development of strategy in an attempt to encourage participation by multiple insurers in the program.
- Difficulties stemming from language in SB 468. Bill contained a variety of specific mandates, including the required bidding process, specific policy provisions (e.g., 25% SIR for CC policies), and definitions of terms that are proving problematic to insurer (e.g., a pollution condition is defined as a release or *threatened* release of hazardous material).
- Change in California administration and re-assessment of overall brownfield program.

### **Anticipated Program Administration**

- State role considered to be vital. State endorsement of program creates expectation of value and consumer protection.
- No funds currently available to administer program; expect that broker will manage administrative functions.
- Data will be collected on extent to which program is meeting needs of insured parties, but details undetermined at this time.

### **Current Concerns about Program**

- Insurer is committing to program pricing at 10% below market. How can the state verify that below-market premium prices are being provided?
- Even though the program is to offer CC for small sites, will it be useful or cost-effective?.
- SL no longer being offered by the selected insurer. How vital is this type of policy to the overall success of the program?

## **Wisconsin's Brownfield Insurance Program (WBIP)**

### **Overview**

- Effort led by Wisconsin Department of Natural Resources (DNR) working with Wisconsin Brownfields Study Group (BSG). Program design and insurer negotiations led by state environmental broker and state risk manager.
- PL and CC coverages proposed; lenders automatically given additional insured status on borrower's policy.
- No state funds designated for subsidies. EPA Brownfields Cleanup and Revolving Loan Fund (BCRLF) may be loaned or granted to subsidize insurance on limited basis for BCRLF participants..
- *Current status: insurer selection process underway. Hope to have contract by December 2004.*

### **Program Development Process and Costs**

- December 2002: State environmental broker selected through competitive bidding process.
- January-August 2003: Broker met with insurers, DNR, BSG, state risk manager to discuss program concept.
- September 2003: Broker submitted specifications to insurers.
- December 2003-January 2004: Interested insurers met with DNR staff to review DNR site assessment procedures and re-opener records.
- March 2004: Initial proposals received from insurers.
- April 2004: DNR/broker submitted questions about proposals to insurers.  
SB 472 authorizing DNR to negotiate and contract with insurers signed by Governor.
- August 2004: Insurers submitted revised proposals.
- Costs to date of program development to state: DNR time.

### **Program Administration Plans and Costs**

- Administration details undetermined, but will be managed by state's broker.
- Specifics of program-related data to be collected not finalized, but broker/insurer contract will have audit provisions to collect information (e.g., premium costs, claims filed and paid).
- Administrative costs to state should be very low. Some EPA 128(a) funds will be used primarily for marketing.

### **Eligibility/Participation Requirements**

- Two categories eligible: Category 1 includes participants in Voluntary Party Liability Exemption Program and those in state's traditional cleanup program who choose to have DNR approve site assessments and Remedial Action Plans (RAPs). Category 2 includes traditional program participants who received Close Out letter from state, which is subject to re-openers. PL coverages requested for both categories; CC requested for Category 1 sites only.
- To participate, applicant will submit application form and financials to insurer. For PL, Phase II assessments required. For CC, state-approved RAP required.

### **Current Concerns about Program**

- Will the discounts offered by the insurer be sufficient to attract developers?
- Will enough parties find the program useful to keep the insurer interested in participating in the program?
- Will pre-negotiated policies adequately fit the risk-management needs of individual brownfield projects?

## Questions about State Insurance Programs for Insurers

**Background of Colorado process.** In March 2004, the Colorado Brownfields Foundation (CBF) organized four stakeholder discussion sessions to examine brownfield liability issues and explore the possibility of pursuing a state insurance program to address them. A number of questions were raised and participants requested that the CBF Environmental Insurance Steering Committee contact insurers. Consequently, the Committee held individual conference calls with six major brownfield insurance carriers in May 2004. Following the calls, key issues were refined. These questions and issues raised by personnel from other state insurance programs are reflected below.

**I. The need for subsidies.** Colorado discussants and individuals from other states maintain that their states are not in a position to offer insurance subsidies. California and Wisconsin are proceeding on the premise that their programs will provide sufficient incentives to spur brownfields reuse without subsidies. The benefits of a state program without subsidies include the following:

- Use of a pre-determined PL pricing schedule helps a developer to assess the feasibility of a project.
- CC policies for small projects are made available (although they may not be cost effective).
- Marketing of the program serves to educate people about insurance as a brownfields tool.
- Pre-negotiated policies save the insured legal expenses and time tailoring policies, an especially valuable advantage to developers who can't afford specialized legal counsel.
- Insurance is offered under state programs at reduced premium prices.

Questions emerge from the last two benefits listed. First, while the use of pre-negotiated policies is considered a major advantage of state programs, no two brownfields involve the exact same risks. Many policies in Massachusetts still need modifications or 'endorsements' to fit individual projects.

*(A) How much time, expertise, and expense is involved in modifying pre-negotiated policies compared with purchasing policies outside of a state program?*

Premium price reductions rest, in part, on insurer willingness to offer discounts because of the volume of business the insurer anticipates. Without subsidies, fewer developers will use the program.

*(B) In the absence of subsidies, can a state program attract enough users to achieve sufficient discounts from an insurer to make the program attractive to developers?*

*(C) How can we confirm the discounts being offered for policies under state programs, since for proprietary reasons, insurers cannot make their pricing models public?*

**II. CC policies for small projects.** The predominant conclusion across the Colorado discussion groups was that there is a great need for CC policies for small-scale brownfields. While such policies are available under the Massachusetts BRAC program, they are very expensive. *Would insurers be willing to offer CC at lower prices if a state would pay for a certain amount of losses each year on small-site CC policy claims?*

**III. PL policy terms.** Some Colorado discussion group members raised the issue of the sufficiency of typical term limits for PL policies (e.g., one to five years). The value of a long-term environmental policy is that it often takes considerable time for the manifestation of third party claims for bodily injury and property damage. *Would you discuss the adequacy of ways of addressing PL policy term length through means such as guaranteed renewal provisions and automatic/purchased extended reporting periods?*

**IV. Effects on cost of using more than one insurer.** While some state program representatives argue that having two or more insurers competing in a program is key to keeping prices low, others argue that use of a single carrier that receives all of a program's business for a designated period is an important price-reducing factor. *Will greater savings result from using a single or multiple carriers in a state program?*