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CONSTRUCTION LAW/COST OVERRUNS

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Putting a lid on environmental cleanup costs: A 2010 perspective

The pivotal issue in a real estate transaction or on-going remediation program is often estimating the total environmental cleanup cost. EWMA has been providing clients with fixed-price cleanup options for over 15 years. Even during these challenging economic times, and the status of the insurance and financial industries, several options exist to better predict, quantify, and cap, remedial costs.

Traditional Time and Material Proposals

Standard "lump sum" or time and materials (T&M) proposals are generally frowned upon in real estate transactions, as invariably out-of-scope work will arise due to site conditions or emerging regulatory requirements. It is generally the lowest price option, but often one with hidden, unquantified costs. Both Clients and Lenders demand greater certainty.

Fixed-Scope/
Fixed-Price Cleanups

A very common cleanup option these days is the fixed-scope, fixed-price proposal. It is essentially comprised of a scope of work developed to address unresolved regulatory concerns. It also may include a limited contingency for likely additional work that could arise with respect to further investigation or cleanup of known conditions. With the contingency, the consultant



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can honor a fixed price for the defined scope of work option. Assumptions in terms and conditions are more limited in the Fixed-Scope/Fixed-Price option than that of a standard T&M proposal, thus providing the customer with a greater measure of security than the sometimes misleading, lower-priced proposals commonly issued by many environmental service providers.

Although not absolutely required with a Fixed Scope cleanup, it typically is advisable for customer to consider purchasing a pollution legal liability (PLL or PLS) environmental insurance policy. The PLL policy provides coverage for third party bodily injury and property damage as well as remedial costs for unknown, pre-existing pollution conditions. The cost of PLL insurance generally ranges from \$30,000 to

\$100,000, depending upon the limits and terms of coverage. The \$100,000 estimate is in the range of a premium having a ten-year term and \$1M to \$3M of coverage. Available terms generally range from three to ten years.

Secur-It Guaranteed
Fixed Price Cleanup contract

In a number of cases where site conditions are well documented (or an appropriate up-front investigation has been performed,) a guaranteed cleanup proposal can be generated. The goal of this option is to obtain for the customer complete regulatory closure of a case. The proposal is structured with a target (or likely, anticipated) reasonable worst case cost, plus contingencies, leading to a Total Guaranteed Cost, which, if exceeded, the consultant is contractually bound and must complete the cleanup at their sole cost and expense. An incentive bonus also applies, whereby the customer agrees to share a percentage of the cost savings or balance, should the total job costs come in below the Guaranteed Price.

Working under guaranteed cleanups, the consultant may be comfortable enough with the data to provide fairly exacting costs without the need for expensive cleanup cost cap (CCC) environmental insurance policies,

which provide coverage for cost-overruns of the known conditions. Uninsured guarantees are often the most practical way to go if anticipated cleanup costs are lower than that usually insured by carriers. CCC policies can be provided for cleanups in the \$2M+ range when the consultant has a proven track record with a carrier, although in some cases policies cannot be underwritten unless the cleanup costs are \$5M or higher.

Perhaps the most "iron-clad" of the environmental cleanup options is that of the insured, guaranteed fixed price contract. Under the insured option, both a PLL and CCC insurance policy is attached to a guaranteed scope of work and associated costs to reach regulatory closure. The goal of this option also is complete case closure. Nearly identical to the uninsured option, both a Target and Guaranteed Total costs are provided. 10%-20% insurance co-pays, deductibles, or self-insured retentions will likely apply before coverage comes into play. A 0% attachment point can sometimes be negotiated, meaning coverage occurs once the estimated cleanup costs have been spent. An incentive bonus also applies, whereby the customer agrees to share a percentage of the balance, should the total job costs come in below the guaranteed price. CCC/PLS insurance policy

costs are in the neighborhood of 12% to 25% of the guaranteed total cost. \$200K-\$300K minimum policy premiums are the general rule, but some exceptions do apply. It is becoming increasingly difficult to obtain a CCC policy, and its price is not always cost-effective.

Requirements for
Guaranteed Proposals

In order to develop a site-specific scope of work and associated costs, the consultant will need to review all existing files pertaining to the case and conduct a site inspection. In some cases, data gaps exist, necessitating varying degrees of up-front investigative efforts (\$10K-\$25K is common,) in order to provide the best, most cost-effective remedial proposal with the least contingencies.

All of these cleanup cost options have their advantages and drawbacks. Before a Client decides, it is essential they obtain experienced legal and insurance advice that best suits the nature of the transaction and environmental conditions on the site. Programs are flexible and are tailored to the transaction.

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