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Managing residual risks of land contamination

David Barr explores how environmental insurance can help manage environmental risks of brownfield sites, including providing long term protection from residual contamination risks.

Risk and reward

The successful trading, development and regeneration of brownfield sites requires stakeholders to acknowledge and manage environmental risks effectively to realise the potential returns.

Whilst many risks associated with the project require careful consideration, the management of environmental risks can have a profound effect on the success, or failure, of a development project.

Get it "right" and the developer and investment partners can reap immense rewards. Get it "wrong" and environmental issues have the potential not only to jeopardise any financial gain on the project, but present long-term liabilities to those involved.

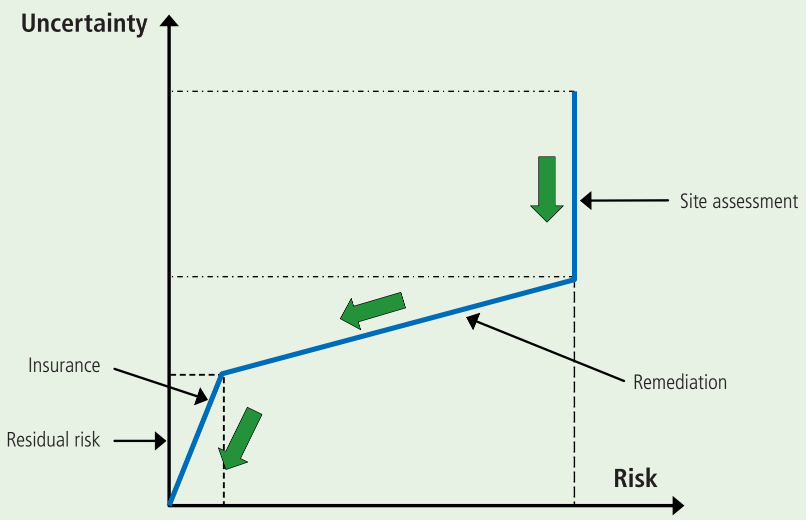
Of course, developers cannot simply adopt a "zero risk" attitude to environmental issues when it comes to brownfield sites, particularly given the current climate of increasing costs of landfilling.

Avoiding sites with actual or perceived environmental risks could result in missed opportunities as a result of deciding not to proceed with a purchase, however budgeting for overly stringent remedial standards during development can risk losing a site to a less conservative competitor.

It is not only major regeneration schemes that require careful assessment. Arguably, the adoption of adequate risk management procedures is even more important for small brownfield sites, where margins will tend to be tighter.

Residual risk and uncertainty

The drive towards the use of "innovative" remediation techniques, particularly those involving the in-situ treatment of soil or groundwater pollution, brings with it the need to address residual contamination risks.



Case study 1
How it can work

A car dealership relocated one of its showrooms, with the intention of selling the site for residential development.

Following the discovery of a widespread plume of petrol contamination caused by a petrol filling station formerly located at the site, remedial plans were prepared in agreement with the regulators.

The petrol plume affected an underlying aquifer, and also extended beneath surrounding residential properties.

The risk assessment reduced the uncertainty to a level that the developer was willing to take on the risk of funding the remediation works, in return for a purchase price reduction.

Although there was general confidence that the remedial works would be successful in reducing both the risk and uncertainty (see diagram left) the developer was concerned that the residual risk exposure could be significant, particularly as they were required to indemnify the seller.

The developer therefore purchased environmental insurance to safeguard against the possibility of future additional clean-up costs or third party claims following completion of the remediation, for example as a result of "rebound" of the plume or future health impacts caused by inhalation of petrol vapours by residents.

Managing residual risks of land contamination

The application of risk-based remediation criteria, whilst an entirely credible and practical solution for modern day brownfield site regeneration, is designed to reduce risks to acceptable levels based on the current status of scientific knowledge, legislation, and (perhaps even more importantly) enforcement practice. Predicting future trends in any one of these factors is prone to significant uncertainties.

One only has to look at the progress made (or lack of it) on Soil Guideline Values in recent years, and the impending Water Framework Directive to realise that this is an area ripe for changes in enforcement practice, raising the spectre of cases being re-opened some years after remedial works have been "signed off" by regulators.

Developers will, understandably, want to realise a profit on their investment as quickly as possible, and will therefore tend to have a relatively short-term interest in a site. Long-tail liabilities associated with residual contamination will therefore typically not be of primary concern.

However, other stakeholders such as investors, lenders and sellers (particularly if the latter are the original polluter) may seek additional safeguards to protect themselves in the event that environmental risks are not entirely addressed through remediation.

In many cases, it may be merely the perception of environmental risk, rather than specific risk factors that cause concern.

Solutions

The increasing availability of fixed price remediation contracts may seem to be the perfect panacea for developers looking to avoid the risk of cost-overrun. But what happens if additional contamination is found that falls outside the scope of the contract, either during or after completion of the remedial works?

The first reaction may be to try to take action against the environmental consultant or contractor responsible for designing and implementing the remediation scheme. This is unlikely to be successful, unless either party has been clearly negligent, or the engineered solution has failed within the warranty period. General liability and property insurance policies will almost certainly offer no protection from ongoing ground contamination liabilities.

By contrast, environmental insurance can offer a cost effective solution to residual contamination risks. Environmental insurance policies cover statutory clean-up requirements, third party claims for bodily injury and property damage, and associated legal expenses, resulting from contamination.

The environmental market has softened in recent years, largely through increased competition, resulting in premium levels being approximately half what they were three years ago for comparable risks. Price is not everything of course, but there is also greater potential to secure coverage enhancements now than in previous years.

Do claims succeed?

In short, yes. Environmental insurance is a relatively young insurance market, nonetheless we are seeing a maturing claims experience in the UK and elsewhere. During a recent survey by Willis, environmental insurers indicated that up to 1 in 10 policies see claims activity, a trend that most insurers agree is increasing, both in terms of the frequency and magnitude of loss.

Case study 2 illustrates a recent example where liabilities of residual contamination, the costs of which ran into six figures, were successfully claimed on an environmental insurance policy.

Whilst policies can be placed quickly and efficiently, it is important to use a specialist broker who is familiar with policy wording, to ensure that any policy placed is tailored to meet the specific needs of the project.

This article first appeared in The Developer's guide to Brownfield, published in March 2007 by Newseye Ltd.

Case study 2
A claim

A landowner implemented remedial works following the discovery of hydrocarbon contamination beneath their site.

The original polluter had ceased trading some years earlier, leaving the current owner liable for the remediation, which was planned and undertaken with the agreement of the regulators.

Upon commencement of the works, the landowner also took out an environmental insurance policy to cover the possibility of additional future clean-up works being required as a result of unidentified contamination being present beneath the site. Due to site access constraints, it had not initially been possible to investigate in all areas.

The remediation achieved the required target, and was duly "signed off" by the regulators, upon which the environmental insurer was obliged to provide for any further "on-site" clean-up costs under the policy terms.

Following this, additional contamination was identified which required further remediation, the costs of which were met by the environmental insurance policy.

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