TURNING TRASH INTO CASH: BROWNFIELD REDEVELOPMENT MAKES "CENTS"

By: Betty Ruth Fox and Todd Jefferson Hartley[1]

"SHOW ME MONEY WITH NO RISK," is the typical response from any developer following a discussion of brownfield redevelopment. Most agree that the reuse of brownfield properties is the right thing to do from a moral standpoint. However, many perceive brownfield redevelopment as a potential financial suicide. This article seeks to explain the typical brownfield redevelopment process and, most importantly, tools available to minimize the risk.

Brownfields exist in every state. For example, in Mississippi alone, the number of reported brownfields is staggering with 1722 known sites catalogued by the Mississippi Department of Environmental Quality ("MDEQ").[2] Many brownfields are never reported and end up escheating to the state or another governmental entity like a county or a municipality. Many brownfields have no actual contamination on the site. Indeed, properties may be classified as "brownfields" simply based on prior uses or potential contamination from adjacent properties. Further, contaminants are not all the same and the risks of some contaminants are managed more easily than others.

Brownfields are often ripe for redevelopment. Brownfields are generally centrally located in areas which have established infrastructure, including transportation systems, water, sewer and other utilities, critical for development. Unlike previously undeveloped sites, other businesses or potential locations for supporting businesses already exist around brownfields. Successful redevelopment of a brownfield also improves tax bases, increases property values, promotes jobs, preserves greenfield properties for the use and enjoyment of future generations, and prevents urban sprawl. Most importantly, brownfield redevelopment positively impacts public health and the environment.

Although brownfields are excellent redevelopment targets, more often than not, the risk of liability from contamination inhibits developers from pursuing these properties. Most states have tried to address this risk by offering protections from liability when certain criteria are met. For example, under Mississippi law, execution of a "Brownfield Agreement" provides liability protection with respect to cleanup costs. Typically state law outlines a method of cleanup of contaminated properties based on the risk posed by the contaminants present at the brownfield.[3] For example, in Mississippi, a brownfield is assessed by an approved brownfield consulting firm[4] which results in the execution of a Brownfield Agreement.

A Brownfield Agreement establishes remediation requirements that are based on public health and environmental risks specific to the brownfield site. A more intensive remediation is required when more contaminants are present on a site or when potential impacts to an especially vulnerable group, such as an endangered species, are possible. Once all remediation goals are approved, liability protection becomes effective. When a developer signs a Brownfield Agreement, no governmental unit at the state level and no private party may require the developer to spend additional money to clean up a brownfield site, unless the agreement is reopened. In some cases, federal action is also barred.[5]

Though state brownfield agreements are strong, "liability protection" is not absolute. A brownfield agreement can be reopened and liability protection can be removed for reasons such as false information, or discovery of previously unknown contamination and risks. Further, additional remediation cost is only one risk associated with the redevelopment of a brownfield. Other risks include lender losses when sites must be remediated, third party claims for personal and property injuries, and disruption to business operations caused by unknown contaminants discovered in the future.

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2 *See* "Mississippi Uncontrolled/CERCLA Sites File List." www.deq.state.ms.us.

3 The Mississippi Brownfields Voluntary Cleanup and Redevelopment Act is a typical state brownfield law.

4 The Brownfield Act requires that consulting firms be approved and listed with MDEQ.

5 For example, in Mississippi, the federal government is barred from taking enforcement action under CERCLA 106(a) and 107(a) against parties who have completed a Brownfield Agreement because of the Environmental Protection Agency's ("EPA") acknowledgment that Mississippi's Program meets the federal requirements of a State Response Program under CERCLA. Note there are several reopeners.

Additional tools exist, however, that are designed to address the various risks associated with brownfield redevelopment.[6] Risk is minimized most effectively by utilizing as many tools as practicable.

1. Corporate Protection

One basic tool to reduce overall risk from the development of brownfields is the use of business entities to limit liability. Similar to typical business transactions, limits on liability through the use of corporate "shell" companies are available in brownfield transactions. Creation of limited liability companies or corporations to limit individual risk is widely practiced. Further, maximum risk protection for the developer of a brownfield site can be achieved by leasing the brownfield as opposed to purchasing the property. This can be accomplished by leasing the brownfield directly from the governmental unit holding title or by leasing from a single purpose limited liability company formed by the developer for the specific purpose of holding title to the brownfield. In either case, the developer leases the brownfield instead of taking title to the property and its accompanying unknown risks.

2. Environmental Insurance

One new and exciting tool in brownfield transactions is the availability of insurance to reduce risk. Traditionally, there has been no market for environmental insurance. In the past, liability for some environmental issues was covered by comprehensive general liability ("CGL") policies until the industry began uniformly excluding environmental liability years ago. Recently, however, insurers have begun quantifying and insuring against the risks of environmental harms. The key to selecting and purchasing environmental insurance is to recognize the complexity of environmental policies and the need for tailoring its coverage to individual projects. Environmental insurance is not standardized or overseen by most state insurance boards. Thus, the best way to utilize these products is to seek out a knowledgeable seller and tailor the policy to an individual circumstance.

Four basic types of environmental insurance exist: Pollution Liability, Cost Cap, Secured Lender, and Finite Risk.[7] Pollution Liability coverage protects against the following: 1) cleanup of previously unknown pollutants on brownfield;[8] 2) bodily injury to third parties caused by pollution; 3) property damage caused by pollution; 4) legal defense costs of third party claims; and 5) ancillary costs. Cost Cap coverage protects against cost overruns caused by higher than anticipated remediation costs. Secured Lender coverage protects lenders from losses due to pollution at properties used to secure loans. Secured lender coverage is triggered by a loan default during the policy period and generally pays the lender the lesser of the cleanup costs for the brownfield or the loan balance. Finite Risk, a less widely available product, protects against cleanup cost overruns, and bodily injury/property damage.[9]

3. Tax Incentives

The federal government has also recognized the benefits of brownfield transactions and has sought to incentivize these transactions and reduce risk through various tax incentives. The most widely available incentive is the brownfield tax incentive which allows environmental cleanup costs at brownfields to be deducted from income. The taxpayer who owns the brownfield can claim cleanup costs as current expenses

6 In addition to the tools listed in this article, various exceptions to CERCLA liability including the "innocent landowner" exception, the "Bona fide purchaser" exception, and the "contiguous property owners" exception also can reduce risk. Discussion of those exceptions is beyond the scope of this article.

7 The four types of policies general specifications:

Name	Risk Covered	Availability	Average Premium	Deductible	Policy Limits	Maximum Term Length
Pollution Liability	Most forms of tort liability	High	$40,000 - $250,000	$25,000 - $250,000	$1 million - $100 million	10 years
Cost Cap	Remediation cost overruns	High	6% - 25% of estimated cleanup cost	10% - 30% of estimated cleanup cost	50% - 200% of estimated cleanup cost	
Secured Lender	Lender losses	Medium	$45,000 - $70,000	$10,000 - $100,000	$3 million - $10 million	10 years
Finite Risk	Tort liability and cost overruns (Loss Shifting)	Low				20 years

8 Also covers "reopener coverage" or further cleanup of previously remediated pollutants.

9 In a Finite Risk policy the insured pays the premium and the present net value of the expected cleanup costs to the insurer who holds the cleanup costs in trust. At the end of the remediation period, the remaining funds in the trust are either refunded to the insured which ends the insurer's responsibility for the site or left in trust which continues the insurer's responsibility for additional cleanup costs.

rather than capitalizing them as long-term assets, lowering income tax on the remediated property. Additionally, many states have state tax incentives which vary by state. For example, Mississippi allows for a twenty-five percent income tax credit for the costs of brownfield remediation. Each brownfield has an annual cap of $40,000 and a $150,000 lifetime cap.

4. Government Grants and Loans

Another way federal and state governments are reducing risk is through grants and loans to developers. EPA site assessment and cleanup grants can be used to fund brownfield site assessment, product and waste inventory characterization, prioritization, community outreach, and cleanup planning and design. For example, the EPA assessment grants can generate up to $350,000 to assess brownfields contaminated by hazardous substances. The EPA has also created the Brownfield Cleanup Revolving Loan Fund ("RLF"). The RLF allows remediation through low or no interest loans for site assessment and cleanup. Other federal grant and loan programs which are potentially applicable to brownfield transactions include programs administered by the Economic Development Administration, U.S. Army Corps of Engineers, Department of Transportation, and Department of Housing and Urban Development.

5. Contractual Protection

Brownfield transactions can also be made less risky through well constructed private agreements. Various classic contractual provisions have been adapted to work in the brownfield transaction context. For example, representations and warranties provisions encourage the disclosure of known risks in order to increase knowledge about the risks associated with brownfields. Key issues include whether predecessor operations on a site are included and the duration of the representations and warranties. Another term, purchase price adjustments, is essentially a formula used to determine the purchase price for a brownfield with the degree of environmental liability as an unknown factor. Thus, purchase price adjustments allow the price of the site to adjust up or down when environmental harms are found to be present or absent. Other contractual terms often used in brownfield transactions include: disclosure schedules; assumptions, retentions, and releases; cost sharing arrangements; conditions to closing; covenants; and indemnification agreements.

In summary, developers and practitioners need to be aware of the risks, and potentially great rewards, of brownfield redevelopment transactions. Layering the liability protection provided by most state brownfield agreements with the wide variety of risk reduction tools available is the best solution to make brownfield redevelopment transactions not only feasible, but economically attractive. ⚖

This article was first published in Mississippi Municipalities, Volume 6, Number 3.