ELI ILF Webinar Series: Financial Assurances

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What are Financial Assurances?

- Mechanism to ensure that:
  - ► Project is completed
  - ► Resources are available to correct or replace unsuccessful projects
- Funds for long-term management are a separate matter
- Long-standing practice in other contexts
  - ► Construction
  - ► Mining reclamation
  - ► Hazardous waste facilities
  - ► Landfill closure

Why Financial Assurances?

- Mitigation projects can be complex and results may be uncertain
- Responsible parties can fail or walk away
  - Bankruptcy
  - Dissolution
- To ensure compensation obligations can be secured on the ground
- Allows at least partial release of credits before project success is demonstrated

In other words…

Financial assurances help us to manage

RISK

Risk can be managed
NOT eliminated!

Requirement for Financial Assurances

- "The DE shall require sufficient financial assurances to ensure a ***high level of confidence*** that the mitigation project will be ***successfully completed***, in accordance with applicable performance standards."

33 CFR 332.3(n)(1)

Financial Assurances vs. Long-Term Management funding

- Financial Assurances help guarantee
  - ►Project is constructed
  - ►Project meets performance standards
- Long-term management funding
  - ►Resources for management AFTER performance standards are met
  - ►Help ensure project is sustainable

When Must Assurances be Posted?

- Permittee-Responsible Projects
  - Prior to commencing permitted activity
- Mitigation Banks
  - Prior to initial release of credits
  - Often in phases
- ILF Programs
  - Funded through credit prices (advance credits)
  - Allocating resources prior to ILF project implementation

When can Assurances be Released?

- Could be held for operational life of project
  (Until end of performance monitoring)
- More often construction & performance securities are phased out as project success is demonstrated
- Permit, plan, or instrument must specify conditions for release of assurances

The Amount of Financial Assurances must

- Be determined in consultation with the responsible party
- Reflect:
  - ► Size and complexity of project
  - ► Degree of completion of project
  - ► Likelihood of success
  - ► Past performance of mitigation provider
  - ► Other appropriate factors

Amount of Financial Assurances

- Based on full cost of providing mitigation
- Could include costs for:
  - ► Land
  - ► Planning, design, and engineering
  - ► Construction & planting
  - ► Monitoring & maintenance
  - ► Reasonably foreseeable remedial work
  - ► Contingencies
  - ► Legal & administrative
  - ► Endowment

Determining Assurance Amounts for ON-SITE Remediation

- Cost to complete work and meet performance standards
- Does **NOT** include LAND COSTS
- High likelihood of successfully meeting performance objectives
- Sponsor provides component cost estimates
- Information sources to verify estimates include
  - Agency in-house engineering estimates
  - Independent third party estimates
  - Current ILF & bank credit prices in service area
  - Similar project costs in same area
  - Software applications

ON-SITE Remediation

ONLY if there are ***NO*** concerns regarding:

- ► Quality of the site & surrounding landscape
- ► Site ownership/access issues
- ► Willingness of suitable third-party to complete work at the site

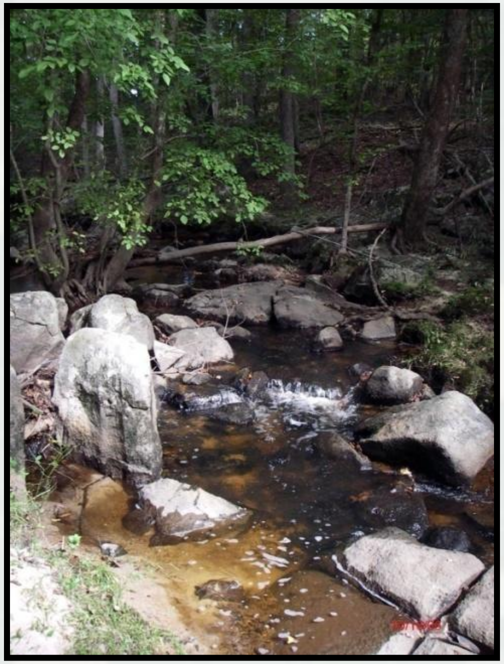
Determining Assurance Amounts for OFF-SITE Replacement

- Costs of compensation at alternative site by a third party
- **INCLUDES LAND COSTS** in addition to other project costs
  - Site does **not** have high potential for successfully meeting mitigation objectives
- Similar sources of information to verify costs as for ON-SITE replacement

Financial Assurances for Preservation Only Banks

EXCLUDE land costs IF:

- ► Site is secured
- ► High value site
- ► No threats to/from adjoining lands
- ► No access issues



- Other costs:
  - ► Physical structures and associated labor
  - ► Surveys
  - ► Legal and administrative costs

Implementing Assurances: Miscellaneous Receipts Statute

- *31 USC 3302(b)* - Money collected by Federal agencies MUST be placed into the U.S. Treasury
- Once deposited into the Treasury it is lost to the federal agency
- Upshot: Federal agencies should not DIRECTLY ***OR*** INDIRECTLY receive assurance payouts because that money will not be available for mitigation

Implications of Miscellaneous Receipts Statute

- Corps cannot be the beneficiary (direct OR indirect)
- Assurances must be payable to a 3rd party ***designee*** of the Federal Agency who agrees to complete approved mitigation project
- Risk of "constructive" receipt

Allowable Forms of Assurances

- Letter of credit
- Escrow account
- Performance bond
- Casualty Insurance
- Other appropriate instruments, subject to agency approval

Letters of Credit

- Financial institution (Bank) extends credit / guarantees payment of sponsor's obligations
- Sponsor pays 0.5 – 1.5% of letter amount to issuer and enters into loan agreement with Bank
- Issues: Limited availability, collateral, provides funds NOT performance, duration

Performance bond

- Contract between sponsor & surety
- Surety guarantees performance OR payment
- Sponsor pays approx 2 - 5 % of penal sum to surety & enters into an indemnity agreement that includes collateral
- Issues: Limited availability, collateral, limits on coverage, potential for performance disputes, duration

Cash in Escrow

- Sponsor deposits entire amount of assurance into an escrow account
- Escrow agent disburses funds based upon notification that specified conditions are not met
- Issues: Cost; provides funds NOT performance

Casualty Insurance

- Only named agency can make a claim
- Trigger is agency determination of default.
- Insurer will satisfy a claim according to approved plan
  - ►Payment to a designee;
  - ►Implement replacement mitigation
  - ►Purchase credits from bank or ILF
- Issue: New assurance mechanism for mitigation (untested)

Claims & Performance:

- Claims require **original agreement *plus* documentation of default**
- LOC and escrow assure **$** not performance
- Beneficiary MUST be identified
- Bonds and insurance offer performance not just money