



MARSH

3E Company HazMat Management Web Seminar Series

“Managing Environmental Risk”

3E Company alleviates the pain of HazMat
Information and Compliance Management

Web Seminar Technology

- Web Seminar audio and visual presented on the Internet
- The preferred screen resolution is 1024x768.
- If you do not have access to Internet, please call 800.207.0148
passcode - 606507
- Click Q&A to submit your questions
- Questions will be answered at the end of the presentation
- If you have any technical difficulties, please email
support@communicast.com
- Web Seminar will be recorded and audio and visual presentation will
be available after the Seminar

Guest Speaker – Janet Carl, Marsh USA

- Environmental Practice Leader, West Region, Marsh USA
- Previous Experience
 - Vice President of Environmental Affairs and Officer - Jefferson Smurfit Corp
 - Practiced Environmental Law – Mayor Day Caldwell & Keeton, TX
 - Lobbyist - Fort Howard Paper, WI
 - Public Affairs Coordinator – Cooper Industries, TX
- Education
 - University of Texas School of Law – JD Degree
 - University of Wisconsin – Platteville – BA Degree, Summa Cum Laude



MARSH

June 24, 2004

3E Company & Marsh Present:

Managing Environmental Risks

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Environmental Practice Leader - West Region
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Overview



- Common types of environmental “risk transfer,” a.k.a. environmental insurance
 - Protection for your operations/properties
 - Facilitate property transactions; provide protection to buyers, sellers, redevelopers, lenders, contractor
- Addressing historical liabilities
- Why attractive to senior management?
 - Hate surprises; love “finality” and “certainty”
 - Their personal liability

Stages of Environmental Risk Management (Remember: “Cradle to Grave” Liability)



Environmental Insurance History

1986

**“Absolute pollution exclusion”
in General Liability policies**

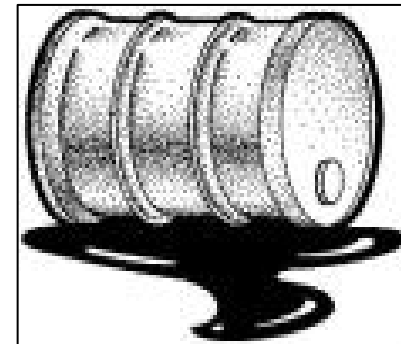


Common Environmental Insurance Structures

- Pollution Legal Liability (PLL)
- Cleanup Cost Cap (CCC)
- Contractor's Pollution Liability (CPL)
- Blended Finite Program
- Insured Fixed-Price Contracting (IFC)

Pollution Legal Liability (PLL): Covers “Unknowns”

- Clean-up costs on-site and off-site for unknown pre-existing contamination
- Third-party claims for bodily injury, property damage - on and off site -- e.g., toxic tort-type claims
- Clean-up costs for new spills and releases
- Regulatory re-openers
- Natural resources damage claims
- Diminution in third-party property value
- 1st-party business interruption
- Transportation of waste
- Non-Owned Disposal Sites (NODs)
- Defense costs



***Typically only available for 10 years**

Safety Net for Operations: PLL Covers Locations Worldwide



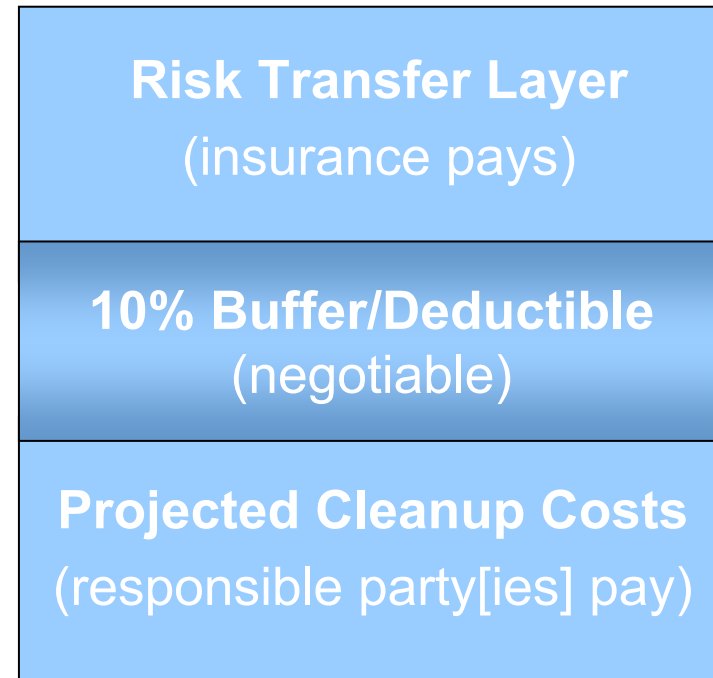
- Semi-conductor manufacturer; 12 locations in U.S., Mexico, eastern European countries, China, Japan, Malaysia, Philippines
 - \$25 M in limits; \$250,000 deductible; 5-year term
 - Coverage for NODs, business interruption
 - Coverage wrapped around government indemnity for one location
- Real estate company; 40 locations: malls, commercial and industrial properties; many divested properties
 - 5 year policy, \$40 M limits, \$500,000 deductible, includes mold coverage, NODs and formerly owned locations

PLL Facilitates Deals; Creates Better Deals

- Semiconductor plant closed in 2002; Seller cleaning up groundwater, will bring site to closure
 - Buyers want to redevelop into industrial park; don't want to rely on seller's indemnity. Buyers secure:
 - \$10 M in limits; 10-year policy, backs up indemnity
- Seller cleans up site; NFA issued; believes property should be valued at \$20 M, getting offers of \$12-\$13 M due to “environmental stigma”
 - Re-marketed with a \$300,000 environmental insurance policy for potential buyer (\$20 M limit for 10 years)
 - Sold property for \$18.5 M

Cleanup Cost Cap: Covers “Knowns”

- Covers cost overruns at the site:
 - More contaminated than anticipated
 - Different kind of contamination than anticipated
 - Remedy failure
 - Change in standards during clean-up
- Typically based on Remedial Action Plan
- Can cover a portfolio of sites
- Typically only available for 10 years



Cost Cap Key to Redevelopment; Facilitating PRP Settlements

- California site; prime for residential development, but contaminated
 - Too many uncertainties; Bankruptcy court involved
 - 10-yr, \$20 M Cost Cap and \$10 M PLL eliminated uncertainties; gave capital investors confidence in project
- 4 PRPs, including the government; \$4 M cleanup
 - One PRP wrapping up operations; wants release from others
 - 10-year Cost Cap and PLL, \$10 M limits, provides more certainty to parties; facilitates settlement

Contractor's Pollution Liability (CPL)

* 60% of contractors have no environmental coverage

Covers:

- Pollution conditions caused, exacerbated by contractor
- Clean-up costs for a newly caused condition, or historical condition that is exacerbated
- Bodily injury, property damage claims, including natural resources damages, loss of use
- Defense costs
- Vicarious liability for subcontractors
- First-party business interruption
- Waste disposal can be covered



CPL Resolves Logjam for Big Box Store



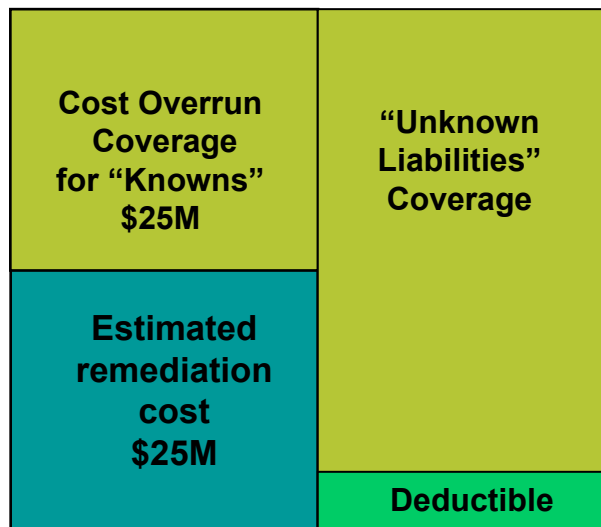
- Builder contracts to build a big box store
- Property has a deed restriction -- contamination left in place
- Builder is afraid of liability that may arise if it exacerbates known contamination
- Store will not give an indemnification
- Builder obtains project policy, \$10M in limits, \$10,000 deductible, \$16,500 premium
- Owner added as additional insured
- Vicarious liability for subcontractors covered under the policy
- Either the “Owner” or the “Contractor” – or both -- can secure environmental coverage for contracting operations

Environmental Coverage Facilitates Light Rail Construction

- City's Light Rail Authority developing 20-mile route through inner-city area, \$500 M project
- Light Rail Authority acquiring full or partial ownership of >500 properties
- Some known contamination; Authority concerned about environmental problems that might arise
 - Many areas bordering state Superfund sites
- Authority concerned the numerous contractors, subcontractors would cause or exacerbate contamination
- Securing CPL and PLL
 - 5-year policies
 - \$50 M in limits

Blended Finite Risk / Risk Transfer

“Pre-Funded” Liabilities with Cost Cap and PLL



e.g.,
20
yrs.

- Attractive for long-term cleanups and long-term O&M
- Takes advantage of discounted net present value dollars
- Shifts timing and investment to financially strong insurer
- Ensures environmental agencies and other parties funding is available for cleanup
- Unspent monies may be refunded
- May have tax, accounting, reserve advantages by accelerating deductibility of remediation expenses (consult tax advisors)

\$25M
pre-funded with
insurance carrier,
@ discounted
present value



Note Regarding Blended Finite Risk Insurance Structures: They All Vary

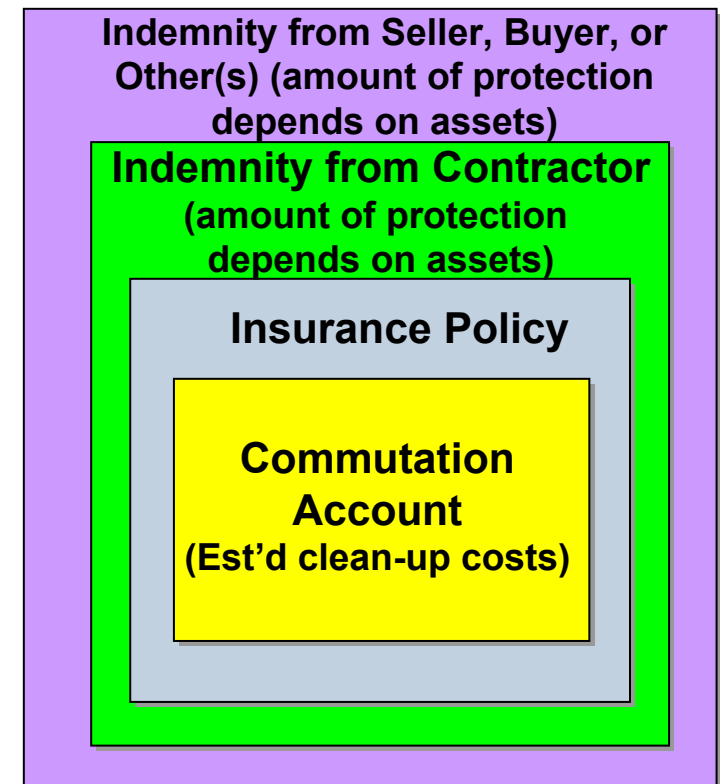
Clients should be aware that "finite risk" solutions consist of a combination or blend of risk transfer and other risk financing strategies. Under certain circumstances auditors and regulators such as the SEC, IRS, and various insurance departments have challenged transactions accounted for as a "finite risk" solution, questioning, for example, whether among other things, there is sufficient risk transfer to support the accounting and/or tax position taken by the client. Marsh believes that finite risk can be a valuable risk management tool. However Marsh makes no representations concerning the proper accounting, legal or tax treatment for any transaction.

Blended Finite Risk Provides “Exit Strategy”

- European company wants to sell U.S. subsidiary; needs “Exit Strategy”
- Subsidiary is PRP at large Superfund site; <10 PRPs
- Buyer says seller’s indemnification alone not sufficient; investment bankers wary
- Seller wants clean-up liability capped; protection for toxic tort, NRD claims, defense costs
- Seller pre-funded cleanup amount (discounted present value), received up to \$250 M in limits for remediation, NRD, tort claims, defense costs
- 27-year term; seller can “commute” after X yrs, i.e., receive remaining funding
- Structure allows divestiture of subsidiary, possibly tax advantages

Insured Fixed-Price Contracting (IFC): a.k.a “Liability Buyout”: No “Defined” Industry Terms

- Clean-ups typically \$3M - \$100M; no two structures identical
- Remediation contractor assumes environmental liabilities
 - May sign onto a consent decree/order
 - May provide broad indemnity
- Carrier acts as the clean-up fund manager, provides cost overrun protection
- Benefits
 - Clean-ups typically cost less
 - Can be done faster
 - Avoids transaction costs
 - May have potential tax benefits (consult financial advisor)



IFC Facilitates Divestiture of Portfolio of Sites

- Company selling subsidiary with several contaminated sites; reserved slightly more than projected cleanup costs
- Company wants to avoid:
 - Major reduction in sale price because of uncertain environmental costs
 - Dependence on buyer's indemnity
- For approx. same cost as it had estimated cleanup, Company secures:
 - contract for clean-up w/ reputable contractor
 - indemnification from contractor, and
 - coverage for overruns and third-party protection, with limits greater than original cleanup projection
- Result: Maximum cost certainty for Company; maximum sale price; avoidance of reliance on buyer's indemnity

Addressing Historical Liabilities

- Drivers:
 - SEC Disclosure, Sarbanes Oxley certification
 - Potential balance sheet improvement (consult your financial advisors)
- Cost Cap and PLL – Petroleum Company: 10-yr policy with \$25 M in limits to cap costs of cleaning up refinery; \$25 M policy to cover third-party claims
- Blended Finite – Midwestern Company: Policy to back up indemnity; recorded as “investments and other assets” in its 2002 MD&A
- Insured Fixed-Price Contracting – Midwestern Company: March 2003 8-K refers to \$39 M liability transfer with a contractor
- Historical GL Insurance Recovery – Fiduciary duty to shareholders
 - Identifying and quantifying the historical insurance asset
 - Recovering environmental costs from historical carriers

Why Environmental Insurance Should Be Attractive to Senior Management

- Increased protection for operations; no environmental surprises
- Facilitate transactions; “cleaner” transactions
- Divest of non-performing assets carried on the books
- Potentially help protect balance sheet (consult with financial advisors)
- Sarbanes Oxley compliance certification; SEC disclosure
 - No material misstatements or omissions
 - Fairly represents financial condition of the company
 - Responsible for establishing/maintaining system of disclosure controls
- **Directors & Officers insurance – typically no Environmental coverage: recent 5th Circuit opinion**
- Provides more **Certainty**; provides more **Finality**

Thank You!!

For more information contact. . .

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