Ecosystems Insurance Associates, LLC
Insurance and Surety

Over $500,000,000 approved and placed

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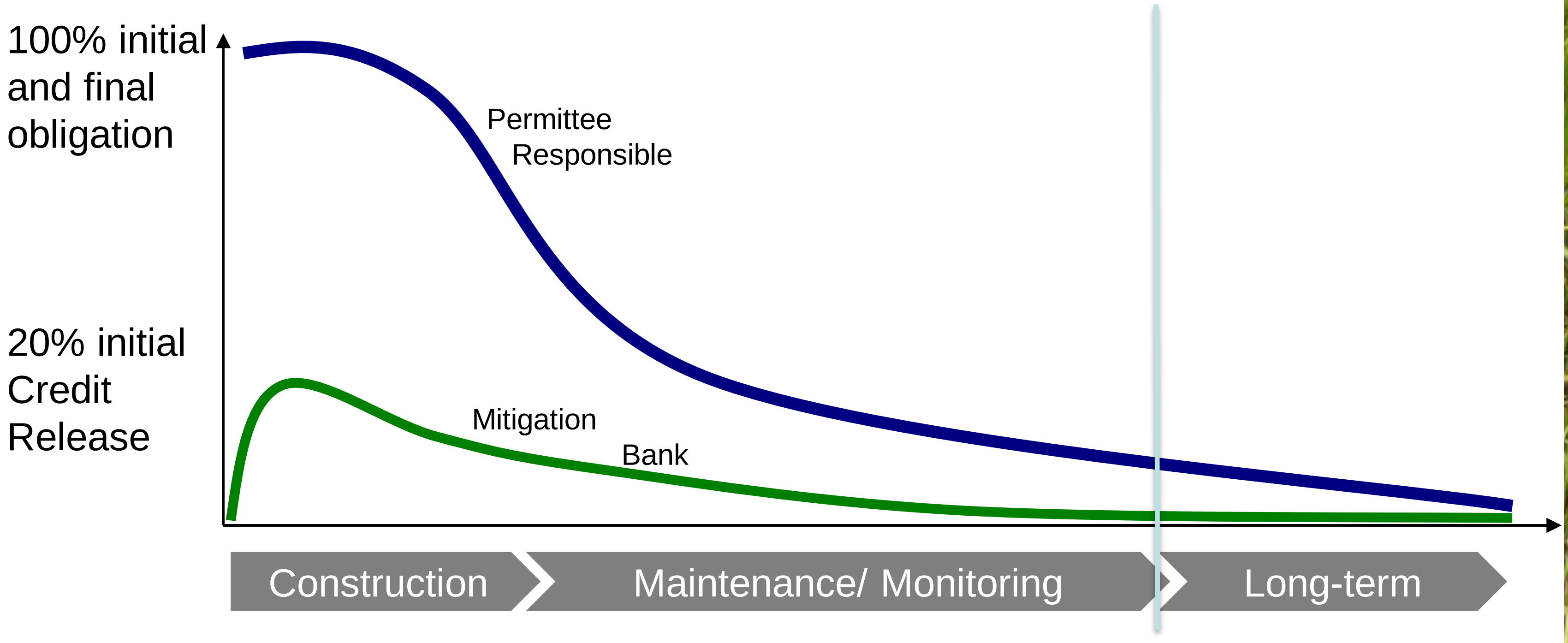
Why Financial Assurance - Generally

Two general types of Financial Assurance:

1. **Uncertain Risks: (Insurance)**
   - "fortuitous" or unplanned accidental events
   - Oil or Chemical Spill, leaching landfill, etc.
2. **Certain Risks (Financial Assurance)**
   - Restoration Obligations
     - Mine reclamation, landfill closure, Oil Wells, etc.
     - Aquatic Ecosystem Restoration
       - Surety Bonds, Escrows, Letters of Credit, Insurance, Corp/Gov't Guarantees.

Performance Risk

Performance risk with scheduled release of credits (Mitigation Bank) or 100% up front (Permittee Responsible or RGL - 1901)



Why? -0- Losses in Mitigation Banking!

- **Built in Regulatory Risk Management …**
  - Adaptive Management
  - Credit Release Schedule
  - Suspension
- **Risk Transfer**
  - The Federal Government cannot and should not take commercial risk, thus requiring Financial Assurance from independent providers is common practice both for “fortuitous and “Certain” risks,
  - Miller Act for Surety,
  - General Acceptance of Insurance and LOC as an alternative to surety.

Regulatory Support

Ecosystem Restoration Financial Assurance

- **Institute or Water Resources**
  - Important "influencer".
  - Studies and recommends but has -0- authority to approve anything. Does not qualify as "Guidance". However, little would get approved without IWR input because it provides necessary knowledge.
- **Chief Counsel's Office, Corps HQ**
  - Engaged with Counsel hired by NMBA (now ERBA) and funded by Ecosystems Insurance Associates and Catlin Insurance Company to draft 1st insurance policy.
  - Drafted 2005 Guidance on Surety Bonds (replaced by 2008 rule but widely followed anyway).
  - Corps Counsel's Office is decentralized. Each District Counsel <u>must</u> also independently approve a bond form or insurance policy and **<u>may</u>** choose to follow Chief Counsel's lead.
- **IRT**
  - In my experience the IRT seldom weighs in on forms of FA, except where there is an agreement to co-regulate with a State DEQ (Jacksonville, Norfolk, etc.).

How Much?

Amount of financial assurance reflects

- Size and complexity of bank
- Likelihood of success
- Past performance of bank sponsor

Amount of financial assurance is based on full costs of providing replacement compensation

- Costs could include:
  - Land
  - Planning, design, engineering
  - Construction & planting
  - Monitoring & maintenance
  - Reasonably foreseeable remedial work
  - Contingencies
  - Legal & administrative
  - Cost of replacement credits (from another mitigation bank or an ILF)

Amount:

- **Most Common:** Construction budget plus a contingency buffer of 15% (as estimated by banker/consultant and verified by agency), then much smaller amounts during M & M period.
- **Less Common:** Cost to purchase credit shortfall from nearby mitigation banks or more likely an ILF (i.e. VARTF in the Norfolk District and the KY ILF in the Louisville District)
- **Amounts Required:** Reduced amount at milestones i.e., approval of “as builts” or M&M report/credit releases.

Timing Issue

- **Corps Perspective:**
  - Conservation Easements, Title Work and Financial Assurance are the final steps in a long process leading to MBI approval/Credit release.
    - This is typically where District Counsel jumps in with respect to a specific MBI.
  - Neither Mitigation Bankers nor providers of FA can demand District Counsel participation – they work solely at the direction of regulators in much the same way outside Counsel is engaged in the private world but with the regulatory side as the client.
  - Corps Counsel and Regulatory resources are constrained resources – both are typically understaffed.
  - Changing the timeline internally can and has been done but requires disrupting the regulatory process and demands internal budgeting/expense approval.

- **Sponsor Perspective:**
  - Leaving discussion of Financial Assurance until the final step can cause significant delays for MBI approval if a new product is presented, even simple variations take time.
  - Seldom will a mitigation banker choose to delay revenue for the purpose of approving a new form of FA. Expeditious approval of an MBI and of a Credit Release is critical to any mitigation banker's business model.
  - That makes it difficult at best for new entrants as providers of FA. It is far more difficult to achieve approval for a new or innovative product than it is to deliver under an existing approved product.

RGL 1901

- **Allows Corps to expedite credit release schedules.**
  - Trade off is an increased reliance on Financial Assurance
  - Language is similar to 2008 rule – i.e. FA must inspire additional confidence.
    - Usually that means that the initial amount of Financial Assurance does not reduce with successful performance reports (M&M reports).
    - Occasionally that also means higher amounts of FA.
- **Some Districts are actively resisting allowing expedited release schedules at all.**
- **Some Districts are applying it selectively – you must demonstrate a need.**
- **Some Districts allow expedited release schedules if applied for in the MBI.**

- **Sponsor Perspective:**
  - It is a good option for Mitigation Bankers because it potentially moves revenue streams forward!
  - Permittees (credit buyers) like the ability to be able to expedite their project permits by having credits available for purchase.
  - Trade off is FA becomes more expensive (even with rate reductions from providers in the out years).

Miscellaneous Receipts Act

Federal Government cannot take non-appropriated funds – they go into U.S. Treasury.
Directing funds may cross the line - “Constructive Receipt”

- **Solution**
  - Delegate to another regulatory entity:
    - In several states, the Corps shares regulatory responsibility. In those states, the Corps oversees a claim, but the state administers it (i.e. Norfolk, Florida). *Note: Fl is assuming almost all 404 authority.*
  - Insert a functioning entity:
    - Several districts require that the Long-Term Steward be appointed at the inception of the MBI. The LTS must agree to handle a claim on the property subject to the amount of FA.
      - Problem – often that is a Land Trust. Some are well established financially, many are not.
      - It is often difficult and expensive to move the LTS forward. Is expertise imbedded in the LTS?
      - NGO’s, TX Parks & Wildlife Foundation, Virginia Outdoor Foundation, etc.
      - Complication – who manages money in the Long Term Management Fund
        - » Accumulation phase Investment Risk? Performance Risk? Yr 1 - 10
        - » Distribution phase Investment Risk? Performance Risk? Yr 10 – forever!
  - Forms of FA that include a “solution” in addition to financial resources may solve or reduce the problem.

Preference

- **Preference** is entirely individual. We have clients that choose insurance or bonds on a project-by-project basis.
- Simple answer – what gets you to the MBI approval point fastest in the least capital intensive manner?
  - Do you want to sign an Indemnity Agreement? Philosophically it backs an obligation you already have thus does not duplicate your financial obligation.
  - Would you prefer to procure all 10 years up front to limit risk of non-renewal or have the product renew annually to cash flow along side revenue?
  - LOCs require corresponding assets in the bank. If you already have those, simplicity may be best. If you don't, you will probably not want to sequester capital.

- **Corps Perspective:**
  - Regulators must approve your financial assurance, thus have the overall authority.
  - Regulators should treat all forms of mitigation equally with respect to Financial Assurance requirements.

- **Sponsor Perspective:**
  - Mitigation Bankers believe that the requirement for FA is not applied equally for all forms of mitigation
    - PRM projects seldom require FA – only large complex projects.
    - ILF's are held to a different standard.

- **Provider Perspective:**
  - Learn to work within the Corps bureaucracy. Fighting it won't work!

Questions

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