

# Financial Assurances



# What are Financial Assurances?

- Mechanism to ensure that:
  - Project is completed
  - Resources are available to correct or replace unsuccessful projects
- Long-term management funding is 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 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)

- DE MUST receive notification **120 days prior to** expiration/termination

33 CFR 332.3(n)(5)

# 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
  - Prior to commencing permitted activity
- Mitigation Banks
  - Prior to initial release of credits
- ILF Programs
  - Prior to project implementation



# How are assurances established?

- Single assurance for the entire project

*OR*

- Multiple assurances/phases
  1. Construction assurances
  2. Performance assurances
  3. Interim assurances



# When can short-term assurances be released?

End of operational life of project

(End of performance monitoring)

Construction & performance securities may be reduced or phased out as project success is demonstrated

Permit, plan, or instrument must specify conditions for release/reduction of assurances

## 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



# Sample Construction Assurance Estimate

STREAM AND WETLAND RESTORATION SITE ENGINEER'S ESTIMATE				Engineer's Estimate	
Description	Quantity	Unit Measure	Pay Unit	Unit Price	Total Fee
Construction Survey	1	LS	LS	\$3,500.00	\$3,500.00
As-Built Survey	1	LS	LS	\$2,500.00	\$2,500.00
Temporary Construction Entrance	2	LS	LS	\$1,500.00	\$3,000.00
Grading	1	LS	LS	\$45,000.00	\$45,000.00
Invasive Species Control	1	LS	LS	\$5,000.00	\$5,000.00
Woody Debris Structure	13	EA	EA	\$500.00	\$6,500.00
Surface Water Diversion	1	LS	LS	\$12,500.00	\$12,500.00
Sediment Bags	4	EA	EA	\$200.00	\$800.00
Impervious Dikes	5	EA	EA	\$500.00	\$2,500.00
Silt Fence	3200	LF	LF	\$2.00	\$6,400.00
Wattles	100	LF	LF	\$5.50	\$550.00
Temporary Seeding	36	AC	AC	\$750.00	\$27,000.00
Permanent Seeding Wet/Sunny	0.9	AC	AC	\$1,200.00	\$1,080.00
Permanent Seeding Dry/Sunny	2.6	AC	AC	\$1,200.00	\$3,120.00
Bare Root Seedlings	2380	Stem	Stem	\$2.25	\$5,355.00
Fencing	1200	LF	LF	\$4.00	\$4,800.00
Clearing and Grubbing	33	AC	AC	\$1,500.00	\$49,500.00
Clearing Only	3	AC	AC	\$1,500.00	\$4,500.00
Incidental Stone	2	Ton	TON	\$50.00	\$100.00
<b>SUBTOTAL</b>					
Mobilization	1	LS	LS	\$9,185.25	\$9,185.25
<b>TOTAL FEE</b>				<b>Total (Calculated)</b>	<b>\$192,890.25</b>



Courtesy Mike Moxey, Mobile District

# Sample financial assurance estimate

## Monitoring & Maintenance Phase

PRESCRIBED FIRE	\$144,000 (4 burns, 1200 acres @ \$30/acre)
FIRE LINES	\$64,000 (4 burns, 8 miles @ \$2000/mile)
ROAD MAINTENANCE	\$8,000 (10 yrs @\$800/year)
EXOTIC SPECIES CONTROL	\$100,000 (200 acres/yr @ \$50/acre/year for 10 yrs)
MONITORING	\$50,000 (\$5,000/year)
CONTINGENCIES (10%)	\$36,600
<b>TOTAL</b>	<b>\$402,600</b>

## Determining Assurance Amounts for ON-SITE Remediation

- Cost to complete work & meet performance standards
- Does **NOT** include **LAND COSTS**
- High likelihood of meeting success criteria
- Responsible party provides component cost estimates
- Information sources used to verify estimates include
  - Agency in-house engineering estimates
  - Independent third party estimates
  - Similar project costs in same area
  - Software applications

## Assurances based upon 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



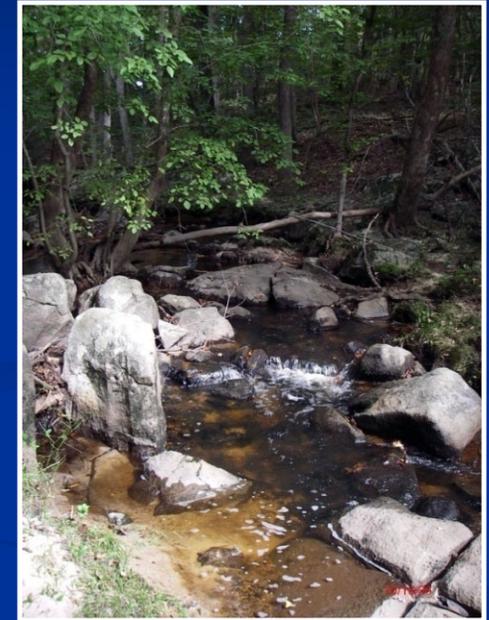
## Determining Assurance Amounts for OFF-SITE Replacement

- 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 Sites

### 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
  - Management costs



# Financial Assurances for ILF Programs

- Conventional assurances (bonds, LOCs)
- Self Assurance – setting aside funds
- Alternate mechanism
  - Letter of commitment
  - No financial assurances required for mitigation projects



## 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 3<sup>rd</sup> party **designee** who agrees to complete approved mitigation project, **or** to a **standby trust**
- Risk of “constructive” receipt



**\* Several districts are identified as beneficiary  
in assurances (LOC)**

**BUT**

- Proceeds will NOT be paid to District but to its designee
- Assignment agreement allows District to specify a designee responsible for developing and implementing a plan

Mitigation provider should identify beneficiary acceptable to IRT

Potential beneficiaries include:

- Government agencies
- Quasi government agencies
- Non-profit conservation agencies
- Land Trusts
- Private entities (in some states)

When evaluating proposed beneficiaries consider:

- Reputation
- Qualifications
- Experience & track record



# Sample Letter of Credit



**Royal Bank  
of Canada**

One Liberty  
165  
New York, NY 10048  
Telephone (212) 850-0100

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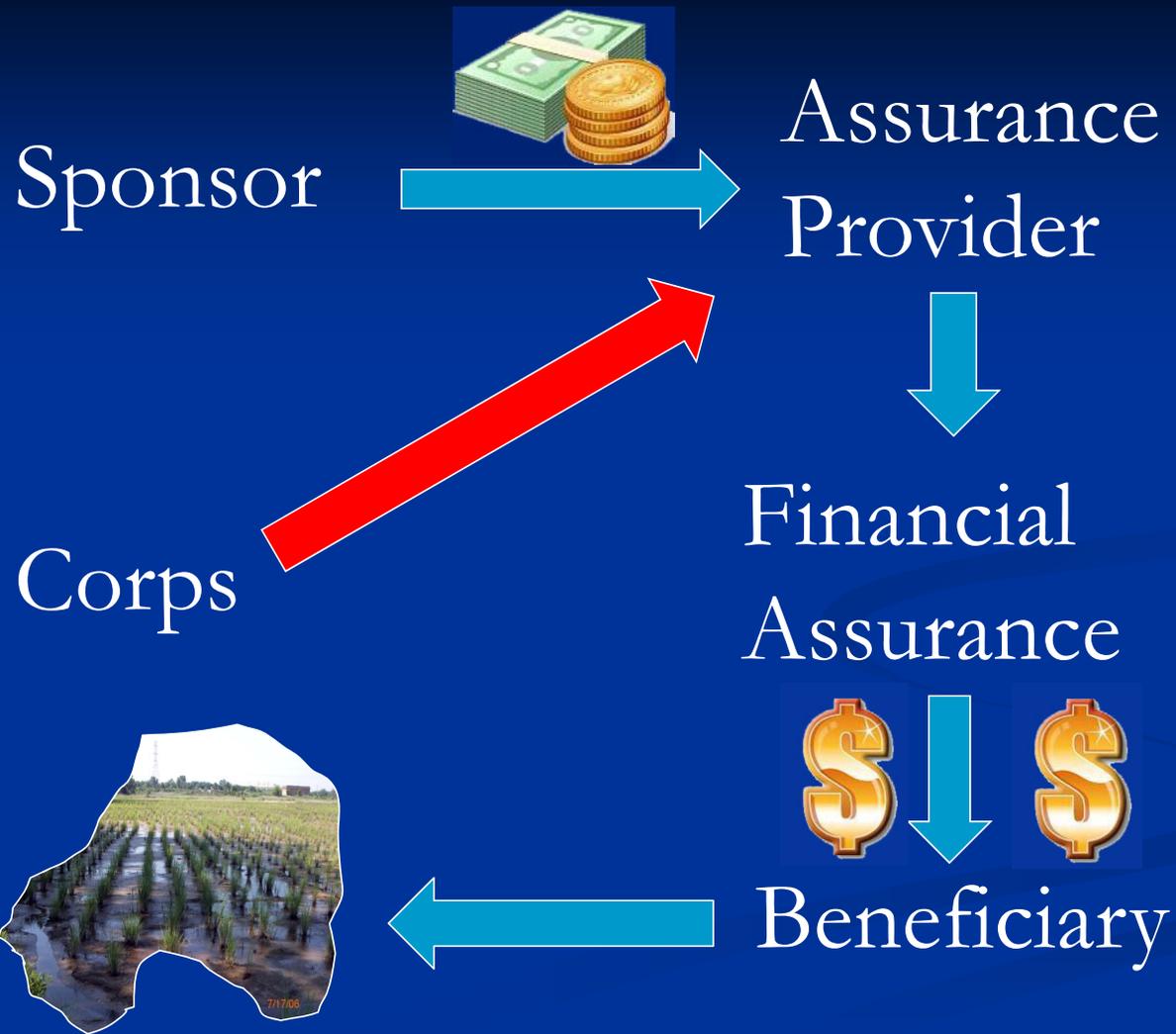
Irrevocable Standby Letter of Credit No.:	1135/S24605
Date of Issue:	October 16, 2009
Currency and Amount:	USD584,916.00
Expiration Date:	October 19, 2010
Place of Expiry:	At our Office

<b>BENEFICIARY:</b> Greatland Trust P.O. Box 101272 Anchorage, AK 99510-1272 Tel.: (907) 278-4998	<b>APPLICANT:</b> Semco Energy, Inc
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# Allowable Forms of Assurances

- Letter of credit
- Escrow account
- Performance bond
- Casualty Insurance
- Appropriations
- Other appropriate mechanisms, subject to district approval





# Letters of Credit

- Financial institution (Bank) extends credit / guarantees payment of sponsor's obligations
- Sponsor pays 1.5-3% of letter amount to issuer and enters into loan agreement with Bank
- Issues: Limited availability, collateral, provides funds NOT performance, beneficiary, duration, *retain original letter*

# Letters of Credit

- “Evergreen” letter of credit:
  - *Expiration date shall be automatically extended...unless at least one hundred and twenty (120) days before an expiration date we notify you ... that we have decided not to extend this letter of credit for any additional period*
- Irrevocable

# 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 performance disputes, duration, *retain original bond,*

# 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; beneficiary



# Casualty insurance

- Insurance policy specifying conditions for payment
- Contract between sponsor & insurer for claims made against the policy up to specified limit
- Sponsor pays one-time premium of 2-10% of cap and agrees to deductible (\$5-50K) for each claim
- Coverage for up to 10 years

# 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
- Issues: Qualifying insured, new assurance mechanism ,  
(untested in mitigation context)

# Standby trust agreement

- Independent third party with fiduciary responsibility to the beneficiary
- Federal agency cannot be the beneficiary (direct OR indirect)
  - Exception discussed on slide 22
- Relationship established through a valid but unfunded agreement
- Enduring
- When assurances called, funds are paid into Standby Trust

# Legislative Appropriations

- Legislative body appropriates funds to guarantee construction & performance
- Identifies duration of assurance
- In event of default/deficiency the mitigation provider would draw on funds to correct deficiency
- Issues: Few examples, generally local government, duration, potential for disputes over performance

## Alternative Mechanisms

- Accept assurance required by other regulatory agencies (*“Me too”*)
- Permit special conditions
- No required assurance



## Alternative Mechanisms – Accept Other Required Assurances

Accept assurances required by other regulatory agencies (“Me Too”)

No issue with Misc. Receipts or beneficiaries

Issues: Corps cannot press claim; Corps has no say in determining compliance or in termination or modification of assurance

## Alternative Mechanisms – Permit Special Conditions

### Permit special conditions

- Typically small projects
- Relies on permit compliance
- Failure to comply triggers alternative mitigation (bank or ILF credits)

Issues: Burden on district to track permit compliance;  
Untested

## Alternative Mechanisms – No required Assurances

Posting assurances not required

- Public (state) agencies with strong record of performance

- Sideboards

- Operating solely as public entity
- Mitigation project fully funded through legislative appropriations
- Demonstrate constitutional, statutory prohibitions on conventional assurances

## Claims & Performance:

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

# Agency Considerations

- Considerations for evaluating proposed mechanism include:
  - On-site remediation or offsite replacement
  - Availability/affordability to mitigation providers
  - Term & renewal issues
  - Ease of access to funds & performance considerations
  - Beneficiary
  - Financial stability of assurance provider
  - Agency experience

# Take Home Messages

- Number of financial assurance options are available
- Mitigation provider is responsible for proposing assurance
- Assurances limit but CANNOT eliminate risk of failure
- Corps cannot be the beneficiary of assurances but can approve plans
- Counsel and staff with experience in establishing assurances can help
- Work on assurances should begin well before the permit, plan, or instrument is completed