How to Divest Environmental Risk

An In-Depth Look Into the Role of Environmental Liability Transfers During Corporate Divestitures

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An In-Depth Look at Environmental Liability Transfers (ELTs) During Corporate Divestitures

The pace of change in market conditions today is moving at unprecedented speeds. New industrial technologies and cleaner energy solutions are forcing well-established corporations and traditional energy providers to pivot to accommodate new market realities and demands. The shift to cleaner and more-efficient solutions is a good thing, but the transition is leaving behind thousands of acres of environmentally-contaminated land and facilities severely impacted by decades of operations. These environmental liabilities are typically found in oil refineries, coal-fired power plants, steel mills, chemical plants, and similar industries.

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The EPA classifies these sites as "brownfields" and defines a brownfield as "a property, the expansion, redevelopment, or reuse of which may be complicated by the presence or potential presence of a hazardous substance, pollutant, or contaminant." Today the EPA estimates that there are over 450,000 brownfield sites in the United States alone. Not only are these sites a blight to their communities and face restrictions for some future uses by the EPA, they are often located close to highly-populated areas, posing a threat to human health and safety.

Decades ago, the generally-accepted corporate strategy to resolve environmental issues was to install a fence around the contamination and forget about it. Today, most C-suites reject this course of action, and realize environmental contamination is a time-sensitive issue – ignoring it only makes the problem worse.

A Dual Threat

The negative impact that brownfield sites have on corporations should not be underestimated. Unresolved environmental issues pose a dual threat to the corporate property holder: a threat to corporate growth potential and a threat to public health and safety.

For companies facing environmental risks, failure to resolve regulatory obligations can be a burden to new growth today and can represent the potential for environmental crises in the future. From a financial reporting perspective, the presence of unresolved environmental issues poses an unknown risk to corporate balance sheets. Risk-averse boardrooms and investors increasingly favor resolving environmental issues before they result in major financial liabilities and potentially massive environmental damages.

Recent global environmental crises shine a spotlight on the extent of damages environmental issues can cause to human health and safety. When a threat to public health and safety is exposed, the onus is on the property holder—legally and morally—to address and resolve the matter as expeditiously as possible. Environmental crises also can cause immediate and often irreparable damage to public perception and brand equity. A comprehensible and sustainable divestiture of known and unknown environmental risks can be achieved, however some methods are more effective than others.

Ineffective Ways to Divest Environmental Risk

» Creating Subsidiaries to Offload Environmental Liabilities

Creating subsidiaries to offload environmental liabilities does not work and is increasingly frowned upon by shareholders and the general public. While this practice is still commonplace, the long-term viability of these reorganizations is to be determined. This solution does not provide a true walk away solution, since the parent company is still responsible for environmental obligations should the subsidiary default. Investors are looking for corporations with limited or no exposure to environmental risk, and many believe shifting environmental obligations to a subsidiary is not a responsible way to resolve environmental issues.

» Traditional Remediation Services

In an effort to mitigate environmental risk, many corporations choose a traditional "time and materials" remediation strategy. Depending on the extent of the environmental problem, this can be a viable solution. However, time and materials services do not address unknown environmental liabilities and therefore do not represent a true elimination of environmental risk. Additionally, these billing methods often lead to protracted clean-up schedules and an overall increase in cost.

The Effective Solution: Environmental Liability Transfers

Proactive corporations are lowering their environmental risk exposure by divesting environmental liabilities through a strategy known as environmental liability transfers (ELTs). ELTs are unique transactions that allow a corporation to shed environmental risk while jumpstarting the remediation and redevelopment of the site through the private sector.

An ELT combines the value of real estate and environmental liability, then transfers the environmental risk (including all future regulatory obligations) to an ELT provider. By assuming the environmental risk on behalf of a corporation, an ELT provider effectively removes an environmental risk and guarantees site remediation with a fully-funded remedial trust.

The ELT divestiture strategy addresses both threats to the corporate property holder: corporate growth potential and public health and safety. Transferring environmental risk to an ELT provider removes the liability from a company's balance sheet, indemnifies all potentially responsible parties (PRPs), and secures environmental clean-up with a fully-funded trust.

A growing number of companies are shifting their environmental liabilities to outside parties. By transferring environmental risk to an outside party, ELTs provide a complete and sustainable "walk-away" option for companies seeking to divest legacy environmental liabilities. For example, during divestiture an ELT often utilizes a sale-leaseback option to maintain operations.

If the transaction is properly executed, this can be a win-win solution for corporate balance sheets and global sustainability. At Environmental Liability Transfer, Inc., we have found that the demand for these types of transactions has increased in relation to the shift from old energy to new energy.

Benefits to Divesting Environmental Liabilities

» Resolving Hazardous Byproducts of Past Operations

A properly-formed ELT provides a financed pathway for carbon-intensive corporations to guarantee the complete and final restoration of contaminated real estate and eliminate any environmental impacts that may have been caused as a byproduct of past operations. By absorbing the risk on behalf of the property holder, an ELT is often the catalyst needed to jumpstart environmental clean-up.

» Sustainability Compliance

The potential expansion of global sustainability standards reporting took a big step forward during the COP21 conference in Paris in 2015. ELTs provide a way for carbon-intensive sectors to adhere to, and prepare for, what most foresee as an inevitable expansion of transparency in sustainability reporting.

» Increase in Overal Valuation and Share Price

Clients of Environmental Liability Transfer, Inc. have seen immediate and positive impacts from divesting environmental liabilities. One publicly-traded client reported that the transfer of environmental liabilities resulted in improved investor sentiment and an immediate 17% elevation in stock price. While these results are not guaranteed, and vary based on size and scope of company, unlocked capital and upgraded balance sheets win the approval of all company stakeholders and can improve the overall value of a company.

» Guaranteed Fixed Cost Solution

Environmental risk poses an inherently variable-cost problem. An ELT provider will underwrite and quantify the value of the risk and provide a complete and sustainable "walk-away" solution. When transferring environmental liabilities and remedial obligations, an ELT provider funds a mutually agreed upon environmental trust, a fixed-cost solution that guarantees the distressed sites will be fully restored. Any cost overruns are the responsibility of the ELT provider.

» Community Benefits

The ELT divestiture strategy also creates a financed pathway to repurpose the property after environmental clean-up is complete, often leading to an increase in local tax revenue, the elimination of industrial blight, the prospect of more local jobs, and a healthier and safer legacy when an established company leaves a community.

CASE STUDY: Shell Global

Environmental Challenge

After decades of Canadian oil refining, Shell Global found themselves holding 135 environmentally distressed properties throughout Canada. These environmental liabilities consisted of former distribution centers for bulk petroleum products, oil transfer and refining facilities, and other sites impacted by years of petroleum-related business activities. Operations on these sites had ceased, leaving behind a large portfolio of shuttered sites impacted by petro-hydrocarbons.

Shell determined that managing contaminated real estate was outside their core business and decided to seek alternative options.

Environmental Risk Assumption and Real Estate Purchase

Shell began searching for a way to divest these contaminated sites and transfer their environmental liabilities, while at the same time receiving fair compensation for the real estate. Additionally, due to their role in the contamination, Shell wanted to guarantee complete and final restoration, and eliminate any environmental impacts that may have been caused as a byproduct of their operations.

Shell approached Environmental Liability Transfer, Inc. (ELT) for a liability transfer solution. ELT was able to completely indemnify Shell of the contaminated properties. By transferring environmental liabilities and remedial obligations to ELT, Shell was able to receive corporate indemnification, guarantee that these distressed sites were restored, and reallocate capital and manpower to core operations.

The transaction gave Shell the ability to divest non-core, contaminated real estate, transfer the environmental liabilities to a third party, and guarantee clean-up of the environmental conditions.

Environmental Remediation

ELT then tasked their affiliate company, EnviroAnalytics Group, LLC (EAG), with the responsibility of cleaning these properties and bringing them into full compliance with Canada's Ministry of the Environment. EAG entered into a remediation services agreement with Shell Global to address the contamination in accordance with Shell's and the Canadian Ministry of the Environment's requirements, which will allow for full remediation and reintegration of these sites back into productive use.

Sustainable Redevelopment

Remedial work has been prioritized to facilitate the reuse/resale of this portfolio. Commercial Development Company, Inc. is currently performing land studies and market assessments to determine the highest and best use for these sites going forward, which could include a variety of vertical development purposes including light-industrial, commercial, and mixed-use.

Results

By transferring environmental liabilities and remedial obligations to ELT, Shell was able to receive corporate indemnification, guarantee that these distressed sites were restored, and reallocate capital and manpower to core operations.

Conclusion

Many factors are forcing the hand of corporations to effectively resolve or divest environmental liabilities: new environmental regulations, balance sheet strains, pressure from activist investors, internal sustainability initiatives, and more. Stakeholders now realize that ignoring environmental problems can have serious and detrimental effects on a corporation.

Unresolved environmental issues impact corporate growth potential, as well as public health and safety. The ELT divestiture strategy tackles both issues. Transferring environmental risk to an ELT provider removes the liability from corporate balance sheets and secures environmental remediation with a fully-funded trust. This provides the spark needed to transform a brownfield property out of blight and return it to productive use.

About the Author

Randall Jostes founded Environmental Liability Transfer, Inc. (ELT) in 2004 and currently serves as its Chief Executive Officer. Over the past decade, Mr. Jostes has greatly improved the landscape of brownfield remediation and redevelopment in North America by successfully assuming and repositioning over $1 billion USD in environmental liabilities. His innovative approach has led to win-win solutions for environmentally-impacted real estate, helping clients navigate the complexities of environmental liabilities and improve their bottom line.

About Environmental Liability Transfer, Inc. (ELT)

Environmental Liability Transfer, Inc. (ELT) is a comprehensive environmental liability acquisition company providing its clients complete and final environmental liability transference services. With robust financial backing and a unique blend of expertise – real estate, environmental, legal, and insurance – ELT has successfully assumed over $1 billion USD in corporate environmental liability for its clients throughout North America.

Contact ELT

For a confidential discussion regarding your environmental liabilities or to learn more about the ELT option, please contact us.

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