CZCPA Risk Evaluation and Financial Assurance Work Group

Initial Scope Issue #1 Strawman: Standard Financial Assurance Instruments

Summary Overview: The attached table identifies the different types of financial instruments commonly considered for use in a financial assurance context, provides a brief description of each instrument, identifies pros and cons, and identifies the federal programs that make use of them and the extent to which they are used to address compensatory damages and/or third party liability.

Financial Instrument	General Description	Pros	Cons	Alignment with Federal FA Regulations
Trust Fund	A grantor (owner/operator) transfers funds equal to the current cost estimate to a trust fund. The Trustee (financial institution) administers the trust for its designated purpose on behalf a designated beneficiary (regulator). It provides annual valuation statements to the Beneficiary. Funds are immediately available to the Regulator. The Trustee charges fees for administrative services	1. Funds are immediately accessible. 2. Owner/operator no longer has direct access to the corpus of the trust without beneficiary approval. 3. Activities can be reimbursed to the owner/operator for approved activities. 4. Some trusts allow owner/operator to direct investments of the Trust. 5. Generally self-implementing, requires minimal regulatory oversight. 6. Generally best for long-term activities	1. Unless the trust realizes a rate of return equal to or greater than the rate of inflation, the corpus of the trust can erode over time. 2. Can be prohibitively expensive to the owner/operator, especially if the owner/operator is not allowed a pay-in period. 3. Unless/until the trust is fully funded, any withdrawal of principal balance ahead of schedule may yield insufficient funds for future activities.	RCRA Subtitle C (HzTSDs), RCRA Subtitle D (SWMUs), RCRA Subtitle I (UST) SMCRA (Mining), CERCLA, SDWA (UIC), TSCA Compensatory Damages Established templates available
Letter of Credit	A document issued by a financial institution that guarantees payment of a customer's (owner/operator's) obligations up to a stated amount for a specified period of time. Requires the use of a Standby Trust Fund, wherein the stated beneficiary is the regulator.	1. Funds are immediately accessible. 2. Once the LOC is called, and poured into the Standby Trust Fund, the owner/operator no longer has direct access to the funds with out beneficiary approval. 3. Activities can be reimbursed to the	1. Unless the LOC has an auto update provision increasing the face value for changes in inflation annually, the face value may not reflect actual purchasing power at the time of draws. 2. Expense ratio is dependent on company financial health. Can be expensive to the owner/operator,	RCRA Subtitle C (HzTSDs), RCRA Subtitle D (SWMUs), RCRA Subtitle I (UST) SMCRA (Mining), CERCLA, SDWA (UIC), TSCA Established templates available

Financial Instrument	General Description	Pros	Cons	Alignment with Federal FA Regulations
Letter of Credit (cont.)		owner/operator for approved activities. 4. LOCs should be evergreen (auto-renewed) and irrevocable. 5. Generally self-implementing, requires minimal regulatory oversight. 6. Generally best for short- to medium-term activities	if the owner/operator is in poor financial health, and is required to post collateral equal to the face value of the instrument.	
Surety Bond	The Surety provides its financial backing to the Principal (owner/operator) and guarantees the Principal's obligations up to the penal sum of the bond. While the Principal is primarily responsible, if the Principal defaults on its obligations, as described in the bond, the Surety assumes responsibility for payment. The Surety will pursue reimbursement from the Principals. Surety bonds can be performance or financial guarantee (payment). If financial guarantee, a standby trust generally is established into which the Surety pours funds for use by the Obligee (the regulatory)	1. The devil is in the details. Funds are immediately accessible, as long as certain provisions are met consistent with the requirements of the bond. 2. In general, only the obligee can direct draws on the bond consistent with the terms of the bond for obligations approved thereunder. 3. Generally self-implementing, requires minimal regulatory oversight as long as the fundamentals of the bond cover the breadth of activities desired by the regulator. 4. Generally best for short- to medium-term activities, and well-defined environmental activities.	1. Availability tends to be a function of the breadth of obligations covered and intended coverage period (i.e., time). 2. Expense ratio is dependent on company financial health. Can be expensive to the owner/operator, if the owner/operator is in poor financial health, and is required to pay premiums equal to the PV of the future expected stream of costs. 3. Market accessibility of surety bonds is constrained for certain environmental activities.	RCRA Subtitle C (HzTSDs), RCRA Subtitle D (SWMUs), RCRA Subtitle I (UST) SMCRA (Mining), CERCLA, SDWA (UIC), TSCA Third-Party Liability Established templates available
Insurance	Contract between two parties, whereby the Insurer agrees to pay, on behalf of the Policyholder (owner/operator) for claims made against the policy. In general, such	1. The devil is in the details. Funds are immediately accessible, as long as certain provisions are met consistent with the requirements of the insurance policy, including all endorsements and	1. Availability tends to be a function of the breadth of obligations covered and intended coverage period (i.e., time).	RCRA Subtitle C (HzTSDs), RCRA Subtitle D (SWMUs), RCRA Subtitle I (UST) SMCRA (Mining), CERCLA,

Financial Instrument	General Description	Pros	Cons	Alignment with Federal FA Regulations
Insurance (cont.)	claims are made with the authorization of the named insured (the beneficiary).	exclusions. 2. In general, only the named insured can direct draws on the policy consistent with the terms of the policy for activities identified thereunder. 3. Requires regulatory oversight to the extent partial claims are made against the policy for approved environmental activities 4. Generally best for short- to medium-term activities, and well-defined environmental activities that fall within standard policy coverages.	2. Expense ratio is dependent on company financial health. Can be expensive to the owner/operator, if the owner/operator is in poor financial health, and is required to pay premiums equal to the PV of the future expected stream of costs. 3. Market accessibility of insurance is constrained for certain environmental activities. 4. Can be burdensome for the regulator if the span of coverages is extensive, and the policy is claims reimbursement upon approval of the regulator.	SDWA (UIC), TSCA Third-Party Liability Established templates available
Liquid Instruments	The Principal (owner/operator) provides the *liquid* instrument to the Regulator. The instrument is held as an offset to the Principal's obligations. Liquid instruments generally include: Cash, check, escrow accounts, CDs, Treasury/Municipal bonds.	1. Readily available funds 2. Generally best for short-term activities.	1. If not carefully structured, the liquid instrument may be cashed out or canceled by the Principal prior to forfeiture. 2. At the state-level, there is the concern of Miscellaneous Receipts Act provisions.	SMCRA (Mining)
Self-Insurance	The owner/operator provides certification of a Corporate Financial Test (with, in some instances, a Corporate Guarantee). The certification entails compliance with an array of financial metrics, as well as financial reporting	1. Provides maximum flexibility to the owner/operator in so far as funds are not set aside in a dedicated account, nor is the owner/operator required to set aside an environmental reserve. 2. Owner/operator (or guarantor) assumes responsibility for payment of all covered	1. In general, regulator does not have direct access to funds. 2. Generally best for short- to medium-term activities, wherein the owner/operator has demonstrated financial	RCRA Subtitle C (HzTSDs), RCRA Subtitle D (SWMUs), RCRA Subtitle I (UST) SMCRA (Mining), CERCLA, SDWA (UIC), TSCA Third-Party Liability

Financial Instrument	General Description	Pros	Cons	Alignment with Federal FA Regulations
Self-Insurance (cont.)	requirements.	activities in the amounts and timing required.	strength. 3. Past financial performance is not a guarantee of future financial performance, and availability of funds.	Established templates available

CZCPA Risk Evaluation and Financial Assurance Work Group

Initial Scope Issue #2 Strawman: Options for Identifying Existing FA at a Site and Minimizing Duplicative FA in Form or Effect

Summary Overview: The WG believes that Coastal Zone Conversion financial assurance should avoid duplicating existing financial assurances applicable to the site, and address only those elements where existing coverage is absent or insufficient for Delaware's needs. The WG recommends that the RAC consider including a requirement in CZCPA regulations for Applicants to identify existing financial assurance relevant to a site.

Options: The RAC will decide whether or not to require CZCPA Applicants to require information about existing financial assurance relevant to a site. If the RAC chooses to make that requirement, the RAC could: a) require Applicants to identify all existing financial assurance relevant to the site; or b) limit identification to existing financial assurances associated with the site/activities involved with the proposed converted/new use.

Pros: Limiting Applicant reporting of existing financial assurance only to those aspects of the site and site activities involved with the proposed converted/new use would focus the CZCPA process on information most relevant to decision-makers. Proponents of that approach note that the CZCPA is not intended to revisit financial assurance decisions unrelated to the CZCPA process.

Cons: Limiting the reporting of existing financial assurance in the manner described above might require judgement by the Applicant with respect to which portions of the site and site activities are related to the proposed converted/new use. Regulators might, or might not, agree with such decision-making. Providing information about financial assurance related to the entire site and all site activities eliminates the need for that judgment. Further, some issues to be considered as part of the CZCPA process (e.g., sea level rise) might by their nature relate to the entire site.

Additional Information: If the RAC requires Applicants to provide information about existing financial assurance relevant to a site and site activities (or a portion thereof), the WG suggests that the RAC consider specifying minimum information requirements about each relevant financial insurance instrument, including:

- Type of instrument
- Issuing financial institution
- Face value
- Expiration date/time period
- Regulatory authority/reason for which the instrument was obtained
- Conditions under which the instrument may be accessed
- Conditions under which the instrument may be canceled
- All Named Beneficiaries

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Initial Scope Issue #6 Strawman: Ensuring DNREC Has Access to FA Expertise and/or Third-Party Verification

Summary Overview: CZCPA decision-makers may not have the internal resources necessary to critically evaluate financial assurance information provided in support of CZCPA permit applications. Options for addressing this issue are identified below.

Options: The RAC could address this issue by: a) integrating third party verification into the CZCPA process; b) charging Applicants a reasonable processing fee for DNREC to directly access financial assurance experts; and/or (c) leverage existing financial assurance expertise from other Delaware state programs with established financial assurance divisions.

Pros: Third party verification is used in the financial assurance regulatory context as a cost efficient and administratively efficient means to minimize the burden on regulators to corroborate all elements of a financial assurance submission (e.g., cost estimates underlying financial assurance instruments, consistency between the form of financial assurance and financial assurance templates prescribed by rule or guidance, attestation to financial condition through financial metrics, financial reports, etc.).

Cons: For third party verification to work, safeguards need to be put in place to ensure that the third party is "arm's length" from the Applicant. One approach is for the state to issue an open call for interested third-parties, and provide each applicant with a list of state-approved practitioners. Or, the state could require certain licensing or practitioner qualifications for the entity providing the verification. Alternatively, DNREC could impose a reasonable application fee, such that DNREC is able to contract with its own financial assurance expert. This practice is similar to that followed by states in their Title V permit programs, wherein Title V requires state programs to be funded solely by fees paid by the subject sources (or applicants).

Additional Information: If the RAC chooses to integrate third party verification into the CZCPA regulatory process, potential requirements for establishing entities as viable third parties commonly include:

- Appropriate licensing, professional qualifications
- A contractor with no existing/other business relationship with the Applicant
- Must be pre-approved by the regulator, or be part of a pre-established list of acceptable practitioners issued by the state.