Expert Commentary

Cost Cap Is Back (and Better Than Before)

After a 9-year insurer hiatus from the market, the marquee environmental product—cost cap—is again available from an A-rated and otherwise outstanding insurer. From roughly 1998 until 2011, cost cap had been offered by AIG, Chubb, XL, and Zurich. It was used to support virtually all of the large fixed-price environmental cleanups throughout the United States. The Environmental Protection Agency (EPA) and other regulators came to love the product, as did industrial owners, developers, bankruptcy courts, and others intent on maximizing cost certainty while avoiding cleanup delays and retaining or even improving cleanup quality.

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Environmental

The New Cost Cap and Its Improvements

Today's cost cap is offered under a new name—Remedial Environmental Site Cleanup Expense (RESCUE)—and improves on even the best pre-2011 cost caps (providing additional coverage and other benefits as well) but, as of this writing, is offered by only one insurer (Markel). Perhaps others will take note and follow suit.

To be considered "cost cap," a policy must cover pollutants that are (1) identified in a government-prescribed remediation action plan (RAP), *and/or* (2) discovered in the course of executing the RAP, all the way through to where the government issues a no further action (NFA) letter. In the absence of the support of both coverages, even the largest remediation contractors have been understandably unwilling to offer fixed price cleanups (FPCs) that meaningfully shift cost overrun risks from the property owners and other potentially responsible parties to contractors. Some contracts professed to do so, but they were either very limited in size (e.g., <$1 million) or allowed change orders that routinely resulted in increased cleanup costs and schedule delays. RESCUE not only provides and further enables meaningful transfers but is *best* suited for sites where cleanup costs are $20 million or more.

Having cost cap back is important as a matter of public interest as well as private. As noted and as the EPA, Department of Defense (DOD), and others have found,[1] when cost caps are integrated with well-constructed FPC contracts, cleanups that routinely result in cost overruns are instead done (1) with maximum cost certainty, (2) on or even ahead of schedule, and (3) with quality meeting or beating expectations. With this record, they should be considered for virtually every cleanup where expected costs exceed $20 million. Some specifics are the following.

1998-2011 (and 2020-forward) Core Areas of Cost Cap Coverage

- Pollutants known at policy inception to require remediation ("knowns")
- Unknown pollutants discovered in the course of remediating the knowns

RESCUE's 2020 Improvements

- Covers off-site disposal and related transportation
- Is in a shorter and otherwise clearer policy (less prone to disagreements, etc.)
- Does not require up-front payment of the expected costs
- In 19 states, qualified projects may be eligible to be written on an "admitted" (versus "nonadmitted") basis, where potential benefits include the following.
    - The limits may be backed by state guaranty funds.
    - There would be no surplus lines taxes and fees.
    - Regulators and others may be more comfortable with the coverage.

As important loss control measures, RESCUE is available only when applied within a comprehensive program that includes the following.

- Robust processes for contractor selection, engineering review, and other due diligence
- A clear FPC contract template that shares definitions and is otherwise closely integrated with the policy
- Post-binding cleanup cost invoice review and other program management from the first month of the cleanup through receipt of the NFA letter

As reflected in my 2016 IRMI.com Expert Commentary on cost caps, alternative forms of cost cap have been applied (via captives and escrows) even during the 9 years that commercial insurers had abandoned the field. Indeed, two such alternatives used by the Air Force (in 2012 and 2015) were not only approved by the EPA but led to its first Federal Facility Excellence in Site Reuse Award.

That said, with cost caps again offered by a large commercial insurer, those who lack a captive and/or otherwise prefer coverage from a large and well-known entity can again get the cost and schedule certainty and other benefits of meaningful fixed price cleanups from such an entity.

Conclusion

While there has been talk of one or two other Insurers entering the cost cap space, until now, none has covered pollutants discovered in the course of doing the cleanup (literally the core requirement), much less offered coverage related to off-site disposal and the other improvements discussed above. Regardless of whether others follow Markel's lead (and eventually some will, though to varying degrees), insureds and regulators should strongly consider the new cost cap at virtually every site with expected cleanup costs exceeding $20 million.

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[1] *EPA Should Increase Fixed-Price Contracting for Remedial Actions*, EPA Inspector General, Rept. No. 13-P-0208, March 28, 2013; *Tracking Performance on the Army's Performance-Based Contracts,* DOD, May 16, 2006 (FPCs routinely meet or beat schedule and quality targets and average 21 percent *below* expected costs); Michael Hill, *A Tale of Two Sites: How Insured Fixed-Price Cleanups Expedite Protections, Reduce Costs, and Help the EPA, SEC and the Public, National Environmental Enforcement Journal*, September 2003 (published at the request of the National Association of Attorneys General).