

14 April 2020

CLM.Consultation@epa.nsw.gov.au

Environment Protection Authority
Locked Bag 5022,
Parramatta NSW 2124

RE: ASBG's Submission on draft Financial Assurance Policy and Guidelines Estimating Financial Assurance:

The Australian Sustainable Business Group (ASBG) welcomes the opportunity to comment on the draft :

- [Financial Assurance Policy](#) (the Policy)
- [Guidelines Estimating Financial Assurance](#) (the Guideline)

ASBG is a leading environment and energy business representative body that specializes in providing the latest information, including changes to environmental legislation, regulations and policy that may impact industry, business and other organisations. We operate in NSW and Queensland and have over 100 members comprising of Australia's largest manufacturing companies and other related businesses.

ASBG notes the Policy is based on the use of Financial Assurances (FA) which has been used by the NSW EPA for many years and can be applied as Environment Protection Licence (EPL) conditions. Similar references can be made to the Contaminated Land Management Act 1997 and the Radiation Control Act 1990.

1 Risk Based Tolerance and Financial Risk

Use of a risk-based approach is welcomed in applying the FA. However, the risk method provided can do with some improvements to ensure that FAs are applied where required and more reasonably. ASBG considers there are two basic reasons where an FA is required:

1. The site may not have sufficient liquidity or accessible funds to undertake the work required
2. The site and owners have a history, which indicates that required environmental actions may be ignored or delayed

This approach is not covered well in the Risk Assessment process used in the Guidelines which appears to ignore the financial ability to cover costs as an element of risk and the need for an FA. Consequently, where sites have strong financial positions and are unlikely to ignore or delay required actions a FA should not be required.

1.1 Risk of Financial Stability

ASBG considers the Policy misses the risk indicator of financial stability, as sites with low financial support are at a higher risk of not addressing a required action or known risk. To address this concern the addition to the risk based approach of financial stability can prove useful. It is perhaps best to look at where the owning organisations have strong financial positions to cover the risks / costs of actions required, rather than look at less stable financial positions. A strong financial position should negate the need for an FA, under point 1 above, unless there is evidence that point 2 is of such a concern. A strong financial position can be assessed where the site or organisation with the EPL or licence:

- Is an essential service supported by Government to continue, e.g. certain utilities, power, water, sewage gas etc.
- Can demonstrate a level of capital or access to capital that would clearly cover the FA amount by an acceptable margin.
- Where such capital is directly linked to the site → i.e. there is a direct line of capital support to the site and not shielded with an excessively complex network of corporate organisational arrangements.
- There is a low risk of movement of financial support away from the EPL site or holder.

Therefore, if a site has a strong financial position, the risk is lower as internal funds are can cover the costs that a FA would cover. This assumes the financial position is larger than the cost coverage required. In other words it has a low risk of not carrying out the activities required due to financial constraints. Consequently, the need to cover this risk by a FA is lower.

Inclusion of Financial Stability, in the Polices' risk list, will ensure that Government Enterprises, sites owned by public companies and supported as well as private companies with good balance sheets and straight forward structures (not a complex web of corporate entities) will largely not require a FA.

Financial stability should cover the waste sector. A waste site with good financial stability should not be required to obtain a FA unless it fails in other areas of risk.

R1 ASBG Recommends adding financial stability to the list of risks when considering requiring a Financial Assurance.

1.2 Risk Scoring and Assessment Approach

In principle a risk assessment process is a good means in which to evaluate when a FA should be required. ASBG considers that financial stability should be assessed on its own merits. ASBG is concerned that categorisation as a high risk is triggered for any area where high risk is cited is too blunt and inflexible. There are cases where a large site has one high risk issue but has a demonstrated high financial stability it should not be considered likely to require a FA, but further assessed. Consequently, the table in section 2.3 Risk based approach requires reworking, with perhaps a variation on triggering a high risk category.

The high risks listed in Appendix 1 range significantly in their severity and concern from medium high to very high. Perhaps an additional column is required listing medium-high risks and high-high risks. Additionally, the complexity and scale of the site could also be considered as larger sites are in many cases a combination of smaller operations. One approach to split larger EPL sites from smaller is if Schedule 1 POEO threshold is also similarly included under schedule 3 of the Environment Planning and

Assessment Regulation. Such an approach would clearly identify large EPLs from smaller types such as for trackable waste generation.

Here are other suggested improvements:

- **Category C: Environmental Performance:** The high risk table (column 4) should be a combination of Environmental Risk Category D or E **and**, (not and/or) *one or more penalty, prevention, or show cause notices issued in the last five years*. The other dot points kept as *and or*. ASBG considers that one clean up or show cause notice, especially for larger more complex sites alone, is not a suitable indicator of a high risk.
- **Category B: Extent of Remediation work that may be required:** ASBG considers these cost ranges are also applicable for other FA cost estimates, not just for remediation work. The expense of undertaking the cost estimates in the Draft Financial Assurance Guidelines would have a flag fall price of around \$50,000, of which the verification would consume about 50%. This can easily escalate. Also a coverage of \$1 million or more by the financial stability of the site owner is not that significant for many larger EPL holders. This appears to have been taken into account for site remediation, but should also extend for other actions being considered for a FA or not. This dot point is discussed further in section 2.

R2 ASBG Recommends amending Appendix 1 Risk Categorisation, Table Category C1, High column, to make one or more penalty, prevention, or show cause notices issued in the last five years an additive example in addition to Environmental Management Category D or E and not a stand alone example.

2 Estimating Financial Assurances Issues

ASBG is concerned the cost of determining a FA can be far higher than the cost of a FA for smaller valued FAs. This brings in to consideration the Guidelines are designed for FAs well over \$ 1 million. However, in practice for the waste sector most current FAs are smaller. It is noted that for waste facilities the calculation method in Appendix 2 is applied and not the Guidelines.

A review of bank fees, the cost of a \$1 million FA is about \$30,000 with a \$2,500 set up fee¹. The estimated lower cost of undertaking a cost estimate using the Guidelines is around \$50,000, but could easily exceed \$100,000. This is far higher than the cost of a bank guarantee in the first year for a \$1 million FA. Clearly FAs for less than \$1.5 million the Guidelines carry with them excessive assessment and verification costs compared to the costs. Consequently, ASBG considers lower cost estimation methods should be made available, rather than a one size fits all approach.

R3 ASBG recommends reducing costs for FAs less than \$1.5 million the EPA should:

- ***Use existing cost calculations for the waste sector***
- ***Not require the verification audit process for FAs less than \$1.5 million***

¹ This is based on the [Commonwealth Bank's rates](#). It also does not take into account the costs of tying up other assets to cover the FA amount.

3 Provisions To Permit Voluntarily Actions To Avoid a Financial Assurance

In the Policy's introduction it says:

A financial assurance is not a penalty for contravention of environmental legislation.

While this is true, the Policy should recognise that requirement for a FA will be a financial burden on any businesses and organisation. In this context, a FA is considered a red flag that the site has environmental risks to the extent where the EPA considers these require to be financially covered. As a consequence, businesses, following good commercial practices, will seek approaches to avoid the imposition of a FA. In this context the threat of a FA can be used by the EPA to entice EPL holders to take actions to minimise their risk of being required to hold one. To ensure preferred risk reduction behaviour is the first option, the EPA should clearly spell out the triggers for a site which is under consideration for a FA to enable the site to respond with reasonably to avoid the FA. ASBG notes a similar approach is already working using contaminated land *Voluntary Management Proposals*, rather than face a *Contaminated Land Management Order*.

ASBG understands there will be sites where the risks are already significant as to warrant a FA. These can be split into two areas:

1. Inherent risk such as affecting certain waste management EPLs – certain waste facilities
2. Self developed risks where the site has performed poorly, such as making excessive and or poorly managed stockpiles and or poor storage of wastes, etc.

Even here there is a possibility that point 2 sites (above) should be given the opportunity to act, before the EPA escalates their requirements. This approach is inherent in the negotiation process in varying EPL conditions, however it is not explicit and an underlying intrinsic approach. ASBG considers it can assist both the site and the EPA, in reduced administrative work, in making the voluntary approach a clear method in which a FA can be avoided

R4 ASBG Recommends the Policy or other Guidelines, clarify a voluntary approach to rectification to an environmental issue/s at a site, similar to that of a Voluntary Management Proposal, as a means to avoid a Financial Assurance requirement.

A site subject to a likely FA should be permitted to demonstrate that its financial stability is high and will implement modifications, remediations or other actions to enable it to voluntarily adapt to avoid a FA to the EPA's discretion.

4 Insolvency Risk and Financial Assurances

One area which should be a significant additional risk is insolvency. Failure to cover the costs are the main types of liabilities the FAs should be designed to protect. Costs can include treatment and or disposal of stockpiles of waste or remediation volumes of ground and groundwater or site clean ups, etc.

Queensland introduced its Chain of Responsibility for environmental risks² largely on mines, but can include industrial sites under the QLD [Environmental Protection \(Chain of Responsibility\) Amendment Act 2016](#) and

² [Review of Queensland's Environmental Chain of Responsibility laws](#)

associated changes. Under this framework the key issue was to enable *environmental protection orders* to be issued to 'related persons' where they can be chased for the liability costs.

While this is a different approach from the NSW EPA framework for FAs, it highlights the issue of financial stability and responsibility. Under Queensland's scheme some mining entities are of a high risk level, they cannot be included under the Government's 'insurance scheme' and must arrange other sureties or not be issued an environmental licence. As such there is an issue in Queensland that new entrants and smaller less well funded projects may not proceed, due to the financial burdens placed on them under the Queensland framework. The issue then becomes that should only projects with an appropriate level of financial backing be permitted to proceed in Queensland? A too conservative approach to financial and environmental risk will stop many potentially highly economic viable projects from proceeding. Given the issues of jobs and economic activity required in hard times, the level of risk adversity needs to be carefully balanced with economic and employment concerns.

R5 ASBG Recommends the level and application of FAs needs to be balanced with jobs and broader economic requirements and the environmental risks to be covered under the FA.

4.1 The Recycling Sector and FAs

The recycling sector is especially vulnerable at this stage in their business cycle. If full FAs were to be applied now, on top of other environmental controls this may tip more to insolvency resulting in orphan sites, which should be avoided. Recycling industry, especially the non C&D operators, are facing a perfect storm of limited export markets, waste export bans, very small domestic markets for their 'products' and increasing regulatory burdens such as increased controls on fire risks. Their main financial issue is they are being expected to operate as if the old export markets exist and pays the same, where now they have dried up. EPAs face a significant risk of new orphan sites in this area. Additional costs at this time from FA's on financially high risk business models will require full asset backing to achieve bank guarantees. Consequently, FAs can be the straw which breaks their backs and must be considered.

There have been cases where international companies have walked away from the site, as well as left Australia, leaving significant waste disposal liabilities. A classic example of this occurred in Victoria:

C&D Recycling's site at Lara, Victoria, which held 320,000 tonnes of waste was abandoned and is expected to cost far more than the \$30 m allocated³ to its clean up and management by the Victorian Government. C&D Recycling's insolvency was also triggered by the Vic EPA enforcing fire control conditions on the site, being the straw which broke that camel's back. While the owner was successfully prosecuted, recovery of the needed remediation money was not. The land owner TASCO, South Korean owned, walked away from the land⁴ they owned, worth \$8m, as the liabilities were far in excess of \$30m.

There are many issues to take into consideration in how to prevent a similar event occurring again. Application of a FA is only one part of the answer, but if wrongly applied could result in exacerbation of insolvency and may result in others pulling out of the business due to the additional cost burdens. Obviously good oversight by the regulator or by other independent entities, such as insurance companies should prevent this occurring.

³ See <https://www.premier.vic.gov.au/government-takes-control-of-lara-waste-stockpile/> Media release 30 April 2020

⁴ ABC news <https://www.premier.vic.gov.au/government-takes-control-of-lara-waste-stockpile/>

How to rectify this? NSW Government, and many other State Governments, have benefited from waste levy revenues for many years. In NSW less than 15% of the levy moneys are currently channeled back to the waste sector and its generators. Given the parlous state of recycling in NSW, there is an argument to cover much of their environmental liabilities using the levy money in full or in part. There are two ways to do this:

1. Develop a state wide FA model where insolvencies are covered with either fully funded by the levy or partially by the recycling sites.
2. Require an insurance policy from recyclers where they pay part of the premium and the rest from the levy moneys.

The second option of use of an insurance policy has a number of advantages:

- The insurer will be responsible for payouts and consequently be auditing sites covered to identify risks early. If a site is facing either environmental or financial risks these will be reported to the EPA if the insurance policy is at risk. This auditing will in practice increase the scrutiny of such sites taking the pressure off EPA staff.
- If an unknown event occurs such as a fire or other, which causes the site to close or require remediation, the insurance policy will pay out to much higher values than can be managed under a FA.

Where certain industrial sectors are affected by short term economic hardship similar provisions could be considered.

R6 ASBG Recommends recycling sectors facing current economic hardship be provided with a Waste Levy supported FA, over the short term, to prevent orphan sites and support the sector.

5 Standards Requirements for a FA

ASBG notes table 3 list of standards requirements for a FA, but raises a concern in relation to point 1:

be unconditional (no special requirements to be met when calling on the financial assurance)

In Victoria an attempt was made to issue an insurance policy to cover a waste site's FA requirements. Here the known risks were covered using warrants and the unknowns by the usual insurance policy provisions. A road block to this process was the refusal by the Victorian EPA to provide any clarification to what could trigger the FA call requirements. It seems the position in Table 3 adopts the same position as the Victorian EPA and will create similar road blocks.

There is a difficulty with this position as it affects not just insurance policies, but also bank guarantees and other sureties. There have been cases where Bank Guarantees have been challenged in court based on the triggering event and whether this warranted access to the money⁵. It appears the current approach by the EPA on FA calling requires additional clarification among the providers of FAs.

R7 ASBG recommends the EPA discusses the unconditional access to FAs with the insurance and financial sectors to ensure it is a workable arrangement and will not detract from issuing bank guarantees, insurance policies or other sureties.

⁵ [Bank Guarantees in Practice](#), Holding Redlich 2018 → Read full article to appreciate the issues to avoid court action

6 Legally Consistent Definitions

The Policy splits the coverage of environmental risks into *known* and *unknown* exposures. As the banking, financial and insurance professions deal with FAs they use the terms *fortuitous* (unknown) and *unfortuitous* (know) around Australia and internationally⁶. To ensure a more legally robust Policy it should adopt the legal terms which are better defined in the institutions where FAs and insurance policies are used.

A number of other terms also should be better defined including:

- Environmental liabilities
- Environmental externalities
- Environmental insurance
- Standard cover versus Standardised cover

There may be other terms used which could also benefit from a better definition in a legal perspective.

R8 ASBG recommends the Policy define terms consistent with the financial, banking and insurance sectors and legislation.

7 Use of Insurance Policies in Financial Assurances

ASBG has long suggested the EPA consider the use of insurance policies as alternatives to Financial Assurances in full or in part. The main reason to use an insurance policy in place of a bank guarantee or similar surety is to provide additional variation, fit, competition and choices for EPL holders to use. In 2009, and again in 2014, ASBG wrote to the EPA regarding the use of insurance policies as alternatives to FAs⁷ and refers to the details in this letter supporting the use of insurance policies.

There are a few issues with the interpretation of insurance policies in the Policy document including:

- Insurance is only for *unknown* (fortuitous) incident → this is incorrect as an insurance policy can use [warrants](#) to cover *known* risks and liabilities.
- The [POEO Act s72](#) does permit the inclusion of insurance policies in EPLs, though this is limited. However, if insurance is permitted as a Financial Assurance it could be applied under FA licence conditions under [Part 9.4 POEO Act](#).
- Section 2.5.1 Standard Requirements the EPA intends to apply refers to *general insurance company* and *reinsurance company* as surety bond providers, but does not make it specific that an insurance policy, either fully or in part, can be used as a Financial Assurance.

R9 ASBG recommends the EPA reconsider and specify the use of insurance policies as an alternative either fully or in part (hybrid) to bank guarantees, bonds and other sureties in its Policy on Financial Assurances.

⁶ What Makes a Loss 'Fortuitous'? <https://www.marsh.com/uk/insights/risk-in-context/what-makes-a-loss-fortuitous.html>

⁷ ASBG Letter to EPA - [ASBG's on Financial Assurances and Environmental Insurance 2014](#)

Should you require further information, clarification or details on the submission please contact me on 02 9453 3348.

Yours Sincerely

A handwritten signature in black ink that reads "Andrew Doig". The signature is fluid and cursive, with the first name "Andrew" written in a larger, more prominent script than the last name "Doig".

Andrew Doig

CEO

Australian Sustainable Business Group (ASBG)

T. +61 2 9453 3348

F: +61 2 9383 8916

(PO Box 326, Willoughby NSW 2068)

Email address:

andrew@asbg.net.au

www.asbg.net.au