

# Closing the Deal – Utilizing a Remediation Cost Estimate in the Negotiation Process

By Robert J. Carr, P.E., LEP

There are many risks involved in the transaction of a brownfields property, especially if it is known or suspected to be significantly polluted. High on the list of risks is the unknown cost to remediate the property and the asymmetrical knowledge of the environmental risk between buyer and seller. A properly structured remediation cost estimate (RCE) can provide the key information to mitigate the risks associated with these unknowns.

As one of the most important and overlooked aspects of the environmental due diligence process the RCE (also known as an opinion-of-cost) should be prepared with the same standard of care as the Phase I and Phase II assessments, especially since this document can be used as the primary negotiating tool between buyer and seller. Not only does a properly prepared cost estimate clarify the risks and investment needed to bring an environmentally impaired property into compliance, but it can also pay significant tax dividends for the new property owner.

## **What is a remediation cost estimate?**

A remediation cost estimate (RCE) is a document comprised of two components; 1) a proposed remedial scope of work that will be conducted to bring the property into environmental compliance, and 2) an opinion-of-cost to complete the described activity. The document may contain several remedial options, and may include several remediation goals (i.e. Will site use be restricted to commercial/industrial? Will a deed restriction be in place?, etc.).

The RCE essentially summarizes the outstanding environmental liabilities for a

property, and presents the potential solutions and costs to remove those liabilities and fully recover the property's assets.

To produce an effective RCE, the remediation goals should be clearly defined beforehand by both buyer and seller. Agreement must be reached on the important parameters of remedial action, such as the future use of the property, the regulatory process to be used, the responsible party for the clean-up, and the timeline expected for completion of remediation activities. The remediation schedule should be a top discussion topic, since some remedial methods, such as in-situ soil treatment may be more cost-effective but may take years to complete.

If the RCE is to be submitted to potential lenders, the RCE can be certified, usually by a licensed professional engineer, to meet lending requirements.

## **Types of Cost Estimates**

Cost estimates can vary in degrees of accuracy, from ballpark estimates, to definitive cost analyses. The Association for the Advancement of Cost Engineering (AACE) has published a cost estimate classification system that is widely used in the engineering and construction industry. In the AACE system, cost estimates are broken down into 5 categories, ranging from concept screening estimates (Class 5) where very little site information is available, to definitive construction estimates (Class 1) where detailed engineering data are available. As expected, the accuracy range for each estimate class also varies, from -50% to +100% for Class 5 estimates, to -10% to +15% for Class 1 estimates. Knowing the limitations of the each type of estimate will help determine what type of estimate will best serve your needs.

The type of RCE to be used is determined by the end use of the estimate. Is a rough estimate needed for a purchase decision, or will a more detailed estimate be needed for project financing? For a typical RCE that is used for budgetary purposes, a Class 3 estimate should be sufficient and would have an expected accuracy range of -20% to +30%. This type of

estimate would be based on knowing the specific contamination at a site, including results of soil and groundwater sampling.

### **The Purpose of a Remediation Cost Estimate**

The above heading is somewhat misleading, since there may be several reasons for preparing a RCE. The RCE is often the instrument used in setting the property's environmental liability and in negotiating the final sales price. It can be used to quantify a no purchase decision if the estimate is higher than the maximum bearing cost determined by a prospective buyer. The RCE can also be used to establish an environmental escrow account to be used for property remediation, or used to define the limits of an environmental insurance policy.

However, there is another beneficial use of a (certified) RCE that often goes unused. The calculated environmental liability can be used to reduce the assessed value of the property, and therefore reduce local property taxes. The result is a built-in tax credit for the property. According to Carolyn Nadeau, President of the Connecticut Association of Assessing Officers (CAAO), environmental related property value deductions are rarely requested by property owners. "If proof satisfactory to the local assessor is presented, then the assessor can reduce the property's assessed value based on the presented environmental liability" explains Ms Nadeau. Proof may include an appraisal, a certified opinion-of-cost, investigation reports, or other supporting documentation.

If a property owner is interested in being considered for this tax benefit, discussions with the local assessor should begin as early as possible so the information required by the assessor can be obtained during the environmental due diligence process. If the assessment deduction is granted, then the submitted information, including the RCE, is recorded and filed with the assessor's office. Once the remedial activities have been completed on the property and full value restored, notice is given to the assessor and the

declared environmental deductions are then removed.

A RCE is a technically verifiable and transparent summary of the environmental liabilities on a property. A properly prepared RCE can be an integral tool in successfully negotiating conditions of the sales agreement (including the sales price) for environmentally impaired properties. The benefits of a certified RCE, which may include substantial tax savings, can mitigate the negative issues surrounding the transaction of a polluted site, and help develop a win-win solution to the parties involved.

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