

Remediation Commercial Management: An Integrated Approach to Cost, Tax and Risk

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INTRODUCTION

With the challenging market conditions the industry currently faces, and the increasing complexity of the remaining brownfield sites available for development, it is more important than ever that the commercial aspects of remediation are managed in the most efficient manner possible. Difficult sites which are on the margins of economic viability need all the assistance they can get, ranging from cost-effective remedial strategies and government incentives through to robust management of risks and liabilities. As one of the three underlying principles of sustainability, economic aspects of contaminated land remediation are an important element of the wider sustainable development agenda.

A comprehensive commercial appraisal of contaminated land development should include an assessment of remediation cost, tax (Land Remediation Relief LRR) and risk. These can be carried out separately, but by far the greatest benefit is derived from an integrated approach. The integration of these components into a holistic assessment is the basis of a new and emerging innovative discipline referred to by the author as Remediation Commercial Management (RCM).

COST

The equation below (Diagram 1) is a simplistic representation of the financial model for development on contaminated sites but there are several important points to observe:

- Build costs for many developments are relatively well understood and quantified;
- The factor with the largest potential variation is 'abnormals costs';
- For heavily contaminated or environmentally sensitive sites, remediation costs are likely to form the major component of 'abnormals costs';

- There is an inherent relationship between abnormal costs and the price paid for the land with the former often determining the latter.

Because abnormal costs are so clearly related to project profitability, on which the viability of a development depends, it follows that a comprehensive and reliable knowledge and understanding of the remediation costs is an essential component of the development

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process for contaminated sites. This is true at all stages of the development cycle, but assessment at an early stage – ideally pre-acquisition – will provide the most robust economic case.

TAX

Land Remediation Relief (LRR) is the government incentive scheme for claiming back corporation tax on costs relating to remediation of contaminated land. Remediation costs (which include consultant and contractor costs) net of LRR can be reduced by up to 40% depending on a number of qualifying criteria. In recent changes to the rules of the incentive scheme

(April 2009), HMRC have removed some of the loopholes and tightened a number of eligibility requirements. They have also extended the scheme to cover derelict, as well as contaminated, sites. As a result, it is now more important than ever to get early advice on the structure (sale and purchase agreement) of a proposed land deal involving a contaminated land site in order to maximise the potential for claiming this valuable relief at a later date. A positive consequence of these 'tightening of the rules' is that there is now much greater certainty over receiving this relief. This means that it is the net cost of remediation which can be used in the development appraisal equation to determine the price paid for the land and predict the potential resulting profit.

This remediation cost advice, incorporating an LRR review, can be highly valuable to both purchaser and vendor. Indeed an independent, authoritative assessment can be instrumental in facilitating progress in a land deal where there is a difference of opinion over remediation costs and eligibility, quantity and ownership of incentives such as the LRR.

RISK

Although 'risk' is technically defined as the product of hazard significance and likelihood of occurrence, in the context of remediation commercial management it can mean many different things including environmental, regulatory/technical, financial, business, corporate and development programme. Different advisors have traditionally managed different aspects – lawyers, cost consultants, environmental consultants etc. . . – but arguably the most beneficial approach is an integrated one which considers the complex inter relationships and appropriate mitigation measures in order to derive the optimum solution.

Increased cost certainty will help bring forward the development of more contaminated sites. The process of increasing cost certainty, much like the CLR11 model procedures, is a staged process whereby risk is reduced by a series of steps with increasing levels of detail resulting from increased availability of data and assessment. Although it can be significantly reduced and better managed, it is unlikely that remediation commercial risk can ever be eradicated.

WHICH ASPECTS OF RCM CAN HELP MOST IN BRINGING BACK CONTAMINATED SITES INTO PROFITABLE RE-USE?

Remediation Commercial Management is an integrated assessment of cost, tax funding and

DIAGRAM 1: The intrinsic link between the cost of abnormal and land price will directly affect the project's bottom line. Early prediction & reduction of the abnormal costs will increase competitive advantage and enhance the profitability



risk issues relating to the remediation of a contaminated site. An RCM report should therefore consider each of these aspects from a standalone and inter-relational perspective. By finding the optimum combination of remedial, LRR and risk strategies, a site has the most chance of being redeveloped.

- There should be different levels of RCM reports incorporating cost plans, LRR tax assessment and commercial risk assessments with mitigation measures;

- These reports should align to the stage of CLR11 (the industry model procedures for the assessment of contaminated land) reached and the amount of information available; The remediation commercial manager should seamlessly interface with the other project professionals in the development team as shown in diagram 2 below.

COST –

Most confidence will be created in the economic viability of a contaminated site redevelopment project if:

- Remediation costs are derived from a comprehensive database of market tested data for engineering and treatment technologies;

- There is a consistent and repeatable methodology for the derivation of costs;

- The level of detail in reports aligns to the stages of CLR11 reached;
- Remediation cost consultants can integrate seamlessly into the land development process, working closely with the other professional advisors;

- Where possible different scenarios of remediation costs are presented, best, worst and most likely with percentage probability, list of underlying assumptions and sensitivity analysis applied.

TAX –

- LRR tax assessments are given in relation to the proposed sale and purchase agreement with recommendations for actions to protect/maximise the relief.

RISK –

- A risk register is provided with responsibilities allocated for each risk identified and appropriate mitigation measures recommended accordingly;

As creating confidence again will be an essential component in the recovery of the wider economy, hopefully effective Remediation Commercial Management can play its part in promoting the redevelopment of contaminated-land sites. **Q**

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12 RCM FACTORS FOR BUYERS AND SELLERS OF CONTAMINATED LAND TO CONSIDER

■ COST

1. Is disagreement between parties on the cost of remediation, allocation of cost and entitlement to the LRR benefit causing an impediment to development agreement?

2. Where do remediation cost estimates come from and how are these costs derived, are they precise enough, how independent are they and what degree of certainty do they bring?

3. Have accurate remediation costs been factored into the sale price and the commercial benefits realised from 'selling the site with knowledge'?

4. Land remediation is complex – is the selected remedial strategy providing best overall cost-benefit value?

5. What degree of certainty is there with the price quoted from a specialist contractor? What risks are – and perhaps more importantly – are not covered by the price quoted?

■ TAX

6. If a contaminated-land site is being sold which has not been remediated, is there an assessment of the likely LRR benefit for a prospective purchaser in order to factor this into the sale price and is the sale and purchase agreement structured in such a way as to maximise the future potential of a LRR claim, thereby maximising the value of the land?

7. Is an assessment of LRR factored into the purchasing development appraisal ?

■ RISK

8. Value engineering – is there confidence that every alternative has been assessed for cost-benefit – including on-site, insitu, ex-situ and off-site options?

9. What is the procurement strategy for specialist remediation contractors? Is it competitive tender, early contractor involvement or framework panel and which form of contract is proposed?

10. Once remediation contractors have been procured how are the remediation costs managed in terms of delays, variations stage payments etc?

11. For portfolios of contaminated sites, have framework panels for advisors and contractors been considered? Is there benefit from standard forms of remediation contract?

12. Is there a risk register clearly allocating responsibility by different parties? What happens to the elements of commercial risk which cannot be mitigated by site investigation, risk assessment and remediation? Is environmental insurance an appropriate risk-mitigation option?

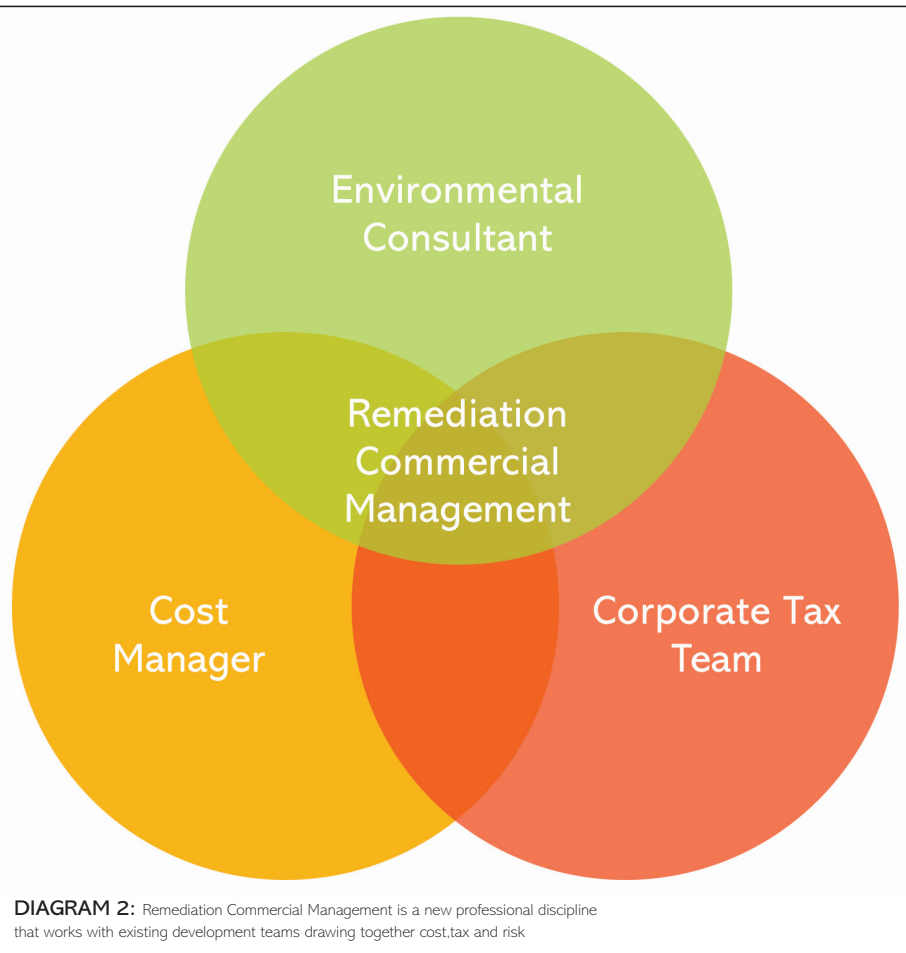


DIAGRAM 2: Remediation Commercial Management is a new professional discipline that works with existing development teams drawing together cost, tax and risk