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Retirement Plan

FIN 47 provides guidelines for recognizing environmental liability costs.

by Dan Johnson, Joseph Kesling, and S. Wayne Rosenbaum, JD

Today companies clean up and sell contaminated property more easily than in the past thanks to new technology and a clear understanding of contaminated property remediation. Many developers and local governments now are comfortable acquiring properties with environmental liability and contamination because potential higher property values after remediation drastically offset clean-up costs. These entities have an appetite for contaminated real estate and are chasing higher rates of return than normally are associated with typical real estate development.

With the introduction of the Sarbanes-Oxley Act and Financial Accounting Standards Board Interpretation No. 47 in December 2005, publicly traded companies now may be required to recognize the long-term retirement costs associated with their properties, including facilities that have been taken out of service. FIN 47 is an interpretation of Financial Accounting Standard 143 or Assets Retirement Obligation. FIN 47's goal is to prompt corporations to properly recognize environmental liabilities on a current basis and decommissioning costs when the property is retired. These companies now have an obligation to book these costs as

they are identified and where the costs reasonably can be monetized. FIN 47 does not impose an obligation to conduct additional assessments or to book costs that cannot reasonably be quantified. However, FIN 47 may cause some companies to decide to remediate equipment or facilities to avoid or lessen the blow of disclosure of any long-term environmental liabilities in their financial statements.

Disclosing the Damage

A 1998 Environmental Protection Agency study revealed that 75 percent of publicly traded U.S. corporations surveyed violated the Security and Exchange Commission's environmental financial debt accounting regulations. Many companies were taking a "don't ask, don't tell" position and did not conduct environmental investigations on their properties.

Many potential environmental liabilities are covered, and they are spelled out in numerous federal and state environmental statutes, laws, and regulations. Examples at the federal level include treatment equipment related to the Clean Air Act, the Resource Conservation and Recovery Act, the Clean Water Act, and underground storage tank regulations.

Remediation Teams

To meet their obligations under FIN 47, companies may wish to engage remediation teams. In addition to a commercial real estate professional, companies need to enlist legal, technical, and accounting help to measure environmental liability. For example, in some high-risk situations, companies team up with firms that offer risk transfer of impaired assets, such as real property that is contaminated, and the related liability. These companies offer protection against the risks associated with long-term environmental liabilities. Such companies can add value to impaired assets by bringing a variety of risk management strategies to bear, including insurance, guaranteed fixed-price remediation programs, liability buyouts, and other risk transfer mechanisms.

When choosing a remediation team numerous factors must be considered including corporate, tax, real estate, and environmental legal expertise; environmental professionals with expertise in remediation, extent of contamination, types of contamination, and available technologies; and accounting expertise. The environmental consultant needs to be proficient in the evaluation of environmentally impaired assets, investigations, compliance auditing and monitoring, risk mit-

igation, remediation, due diligence, and the support of acquisition and disposition of contaminated real estate. The environmental consultant can help develop and implement a strategy to identify, manage, mitigate, and monitor contingent environmental liabilities.

Troubled Real Estate Assets

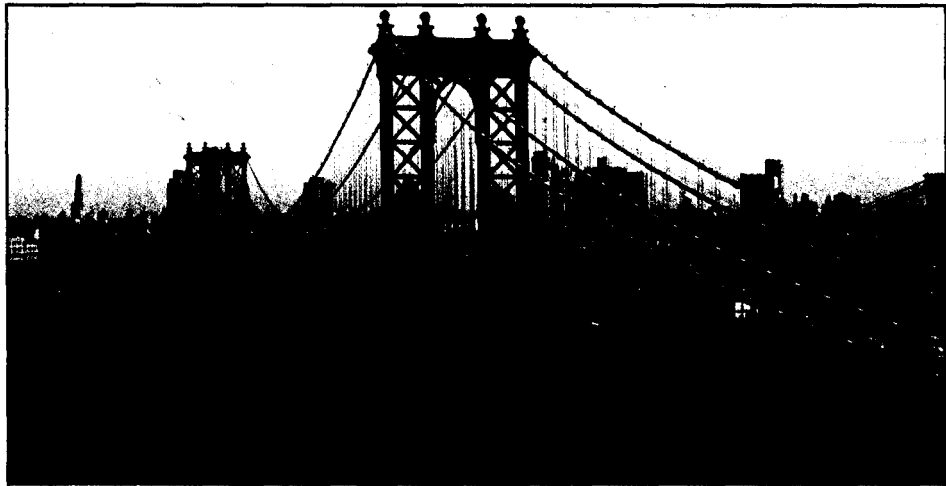
This is a great time in history for companies to divest troubled assets. Aside from many companies looking to acquire contaminated real estate, the new "all appropriate inquiry" standards, which are required under the Brownfields Amendments, required the EPA to define AAI. The standards now are completed and will take effect in November. AAI is a means to an end for the Brownfields Amendments of 2002 and offers enhanced innocent landowner liability protection and new bona fide prospective purchaser and contiguous property owner defenses.

The bona fide prospective purchaser allows a buyer to knowingly purchase contaminated real estate and be protected against unknown or undiscovered environmental liability created prior to the purchase when all appropriate inquiries have been made. For developers these adjustments introduce new brownfield properties into the marketplace. Whereas the company has an obligation to identify and the ability to quantify the future liability, FIN 47 may encourage some companies to sell these assets so they will not have to account for future retirement costs.

There are other factors to consider when selling tainted property, as the sale does not completely release companies of their envi-

ronmental liabilities. A sale does provide cash, eliminate ongoing carrying charges and maintenance budgets for the properties, and reduce future liabilities on the income statement. In the case of environmentally contaminated real estate, the liabilities do not drop away until the site is remediated, but the net effect is that reduced environmental liabilities help shore up and preserve stock values and protect against a credit down rating of the company.

With the proper mix of risk mitigation strategies, recent legislative changes, AAI, and a buyer's market for contaminated real estate assets, a public company finally can start to get control of its contingent environmental liabilities. FIN 47 may help to create these opportunities for companies and developers by prompting companies to assess their retired properties' identifiable and quantifiable costs.



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