Economic Impact Analysis
Virginia Department of Planning and Budget

9 VAC 25-650 – Closure Plans and Demonstration of Financial Capability
Department of Environmental Quality
April 23, 2001

The Department of Planning and Budget (DPB) has analyzed the economic impact of this proposed regulation in accordance with Section 9-6.14:7.1.G of the Administrative Process Act and Executive Order Number 25 (98). Section 9-6.14:7.1.G requires that such economic impact analyses include, but need not be limited to, the projected number of businesses or other entities to whom the regulation would apply, the identity of any localities and types of businesses or other entities particularly affected, the projected number of persons and employment positions to be affected, the projected costs to affected businesses or entities to implement or comply with the regulation, and the impact on the use and value of private property. The analysis presented below represents DPB's best estimate of these economic impacts.

Summary of the Proposed Regulation

State Water Control Law (Section 62.1-44.18:3) requires that owners of a private sewerage system or sewerage treatment works file a closure plan and demonstrate financial capability to abate, control, prevent, remove, or contain any substantial or imminent threat to public health or the environment that is reasonably likely to occur if such a facility ceases operations. In accordance with the State Water Control Law, the proposed regulation requires a closure plan and demonstration of financial capability to implement the plan for privately owned sewerage systems or sewerage treatment works that discharge between 1,000 and 40,000 gallons per day. The proposed regulation has been in effect as an emergency regulation since December of 2000.

Estimated Economic Impact

Prior to the emergency regulations, owners/operators of a private sewerage facility were not required to demonstrate their financial capability to implement a closure plan in the event that the facility is abandoned. The proposed regulation requires that the owners/operators of these facilities submit a closure plan and demonstrate financial capability to implement the plan should the facility cease operations. The closure plan must be approved by DEQ. Regulated facilities include mobile home parks, residential subdivisions, and apartment complexes. Ceasing operations at these facilities is likely to create a public health hazard, as the discharge of pollutants is likely to continue and reach the state waters untreated. To reduce potential health hazards, the owner/operator of the facility is required to submit a closure plan to DEQ. A closure plan identifies the course of action that will be implemented if the facility is abandoned. A closure plan may consist of cessation of the discharge, connection to an alternative facility, transfer of the facility to the local government, contract operation of the abandoned facility by some other entity, or an alternative plan that may be proposed.

The owner/operator of the facility will be required to provide financial assurance to cover the estimated costs of implementing the closure plan. Financial capability may be demonstrated in several ways. First, the owner/operator may choose to establish a fully funded trust. The trustee usually requires a fee to manage the fund that depends on the amount in the fund. The management fee is usually less than one percent. The securities in the fund can earn returns. However, there are opportunity costs involved, as the owner/operator is not free to invest the dollars in other projects that may provide a better return. Thus, the net cost of this method is the fee paid to the trustee and the difference between the potential return that could be earned from an alternative investment and the actual return earned on the fund. Second, the owner/operator may demonstrate financial capability by providing a surety bond. The cost of this method is about one to three percent of the face value of the bond that must cover the estimated cost of the closure plan.[1] For less risky owners/operators, the premium paid to the surety is likely to be lower. The bonding company may require collateral if the owner/operator is very risky. Finally, the owner/operator may fulfill the financial assurance requirements by providing a letter of credit that may be cashed if needed. The cost of the letter of credit depends on the length and the quality of the relationship between the issuing institution and the owner/operator. Letter of credit maintenance fees vary from about 0.75% to 2% of the face amount indicated in the letter.

[1] Source: DEQ

The proposed regulations will require 65 private sewerage facilities to demonstrate financial capability. The cost of financial assurance to the owners/operators of all of these facilities will depend on the estimated closure costs. Implementation of the closure plan is likely to vary significantly among alternatives based on the facility type, facility condition, and the amount of flow. Closure costs are expected to vary between ten thousand to one hundred thousand dollars.[2] A ballpark figure for the total financial assurance costs can be estimated under a specific set of assumptions. For example, if a closure plan costs $40,000 on average to implement and the mean financial assurance cost is 1.5% of that amount, the total cost of 65 facilities to demonstrate financial assurance is expected to be $39,000 per year. However, this estimate is subject to uncertainty since neither actual closure plan costs nor financial assurance costs are known at this time.

The owner/operator of a private sewerage facility may be able pass some of the financial assurance costs to their tenants. The degree, the owner/operator can pass additional costs depends on the local market conditions for residential real estate. In areas where vacant residential spaces are relatively abundant, the owner/operator is likely to incur most of the burden. Conversely, in areas where the housing market is tight, tenants are likely to incur most of the burden.

Some staff time will be devoted to analyze the plans and financial documents of 65 facilities submitted for approval. DEQ does not have an estimate on the amount of staff time that will be required but expects it to be small. One time staffing needs at the beginning of the program are likely to be relatively more than the ongoing staffing needs.

In cases where the ownership of the facility is transferred, the old and new owners are likely to incur some additional burden. This is because the proposed regulation requires the old owner to notify DEQ at least 120 days prior to the sale of the facility. This requirement has the potential to effectively delay the transfer of ownership for at least four months. The mandatory delay of ownership is likely to interfere with the timely business plans the old and new owners may have. The justification for required notification is to inform the new owner that financial assurance will be required when the facility is bought so that he is aware of the additional costs. It appears that the choice of 120-day notification is arbitrary and could be reduced to the benefit

[2] Source: DEQ

of both the old and the new owner of the facility. Reducing the required number of days prior to sale for notification and still achieving the intended goal of the regulation seems feasible.

The benefits of the proposed regulation include ensuring that the funds will be available to implement the closure plan if a private sewerage facility is abandoned. Prior to the emergency regulations, if an owner/operator abandons the facility, state funds may have been used to pay for the closure costs. Additionally, under the proposal, some financially unstable owners/operators may be forced to sell their facilities to more financially secure entities due to their higher assurance costs. Some other financially weak entities will be discouraged from buying these facilities because of additional costs. Thus, by ensuring that the funds will be available to implement closure plans and by decreasing the number of owners/operators incapable of paying their share of closure costs, the proposed regulation decreases the likelihood that state funds will be used for that purpose. The case of Queen Annes Court sewage treatment plant may provide an example to illustrate the potential benefits of the proposed regulation. In 1999, the treatment plant was abandoned. Consequently, DEQ paid $32,018 to Hampton Roads Sanitary District to operate the plant for about 10 to 11 months and deactivate the plant after completing a pump station to divert the flow to a public sewer.[3] If financial assurance had been required, state funds would not have been spent.

Ensuring the availability of funds for closure and reducing the number of owners/operators that are not financially strong would likely also reduce delays in facility closure and prevent discharge of untreated pollutants to the state waters. Thus, the proposed regulation has the potential to reduce the facility closure failures and delays which would be beneficial for the environment as well as for third parties that may be subject to potential health risks.

In summary, the benefits of the proposed regulation include the assurance that funds will be ready for the timely closure of an abandoned privately owned sewerage facility. State expenditures on the abandoned facility closure, damage to the environment, and risks to the third parties could potentially be reduced. Demonstration of financial capability will involve net costs

[3] Source: DEQ

for owners/operators. Though it seems likely that the potential benefits exceed the potential costs, there is not enough information to support that conclusively.

Businesses and Entities Affected

The proposed regulation will affect the owners/operators of 65 privately owned mobile home parks, residential subdivisions, and apartment complexes. If the owner/operator is able to pass financial assurance costs to the tenants, tenants living in these facilities will also be affected in terms of slightly higher rental costs.

Localities Particularly Affected

The proposed regulation will affect localities throughout the Commonwealth.

Projected Impact on Employment

Due to higher costs of operating a residential facility with an independent sewerage system, a few owners/operators may be forced to shut down their businesses. This may have a small negative impact on employment; perhaps, a few positions in property management will be eliminated.

Effects on the Use and Value of Private Property

The value of the 65 residential facilities that are subject to the proposed regulation may decrease by a small margin due to additional costs.

Some businesses that provide financial assurance for profit may enjoy a small increase in value as their business volume is expected to increase. Private properties where immediate health risks may accrue due to facilities discharging untreated pollutants to adjacent waters may experience a small positive impact on their values. This is because potential buyers are likely to add the discounted value of reduced health risks in the future to property's present value.