

# Types of financial assurance

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EPA acknowledges Aboriginal people as the first peoples and Traditional custodians of the land and water on which we live, work and depend. We pay respect to Aboriginal Elders, past and present.

As Victoria's environmental regulator, we pay respect to how Country has been protected and cared for by Aboriginal people over many tens of thousands of years.

We acknowledge the unique spiritual and cultural significance of land, water and all that is in the environment to Traditional Owners, and recognise their continuing connection to, and aspirations for Country.

### Disclaimer

The information in this publication is for general guidance only. It does not constitute legal or other professional advice and should not be relied on as a statement of the law. Because it is intended only as a general guide, it may contain generalisations.

You should obtain professional advice if you have any specific concern. EPA has made every reasonable effort to provide current and accurate information, but does not make any guarantees regarding the accuracy, currency or completeness of the information.

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## Purpose

This document gives an overview of types of financial assurance that Environment Protection Authority Victoria (EPA) may consider and when each type of financial assurance may be applied.

## Legal status

This guideline provides duty holders who have to submit a financial assurance with information about the different types of financial assurances that EPA may accept under section 67B(1) of the *Environment Protection Act 1970* (the Act).

EPA is responsible under the Act for determining the type and extent of a financial assurance.

## Introduction

EPA requires duty holders operating certain scheduled premises to provide a financial assurance. Under the Act, this requirement can be specified in a works approval, licence or a pollution abatement notice as well as a waste transport permit.

The types of scheduled premises that may be required to submit a financial assurance are specified in Schedule 1 of the Environment Protection (Scheduled Premises and Exemptions) Regulations 2017. Financial assurance may be applied to landfills, Prescribed Industrial Waste (PIW) management, PIW composting, container washing, bulk storage facilities, contaminated land – onsite soil containment, and contaminated land – long-term management.

Generally, EPA has required duty holders to provide bank guarantees as financial assurances. EPA expects that it will continue to require bank guarantees as the type of financial assurance in most cases, however other types of financial assurance may occasionally be appropriate. Before making a determination under Section 67B(2) of the Act, the Authority will generally notify the duty holder of the type of financial assurance that is likely to be determined.

Legal documentation may be required to establish the financial assurance instrument in some cases. Costs associated with utilising non-standard types of financial assurance, including costs incurred by EPA for preparation or review of legal documentation for individual proposals and advice from external service providers, must be borne by the duty holder.

This document outlines what each type of financial assurance under the Act means, as well as other types of financial assurance EPA may consider.

Related publications that may assist include:

Publication 1594: *Financial assurance for licences and works approvals*.

Publication 1596: *Calculation of financial assurance for landfills, Prescribed Industrial Waste management (PIW) and container washing*.

## Bank guarantee

A bank guarantee is an unconditional written undertaking issued by a bank in favour of EPA, in which the bank promises to pay a certain amount of the bank customer's money upon demand by EPA.

Bank guarantees are the most common form of financial assurance.

Bank guarantees:

- specify a dollar amount that will be paid upon demand
- pay unconditionally
- are perpetual
- are administratively simple.

### How it works

After the duty holder enters into a contract with a bank, the bank guarantee is provided to EPA by the bank. Generally, the contract between the duty holder and the bank involves a security of cash or assets together with payment of regular premiums to the bank, in return for the bank providing the bank guarantee.

Any bank that issues a bank guarantee must:

- be regulated by the Australian Prudential Regulation Authority (APRA) or be based in a country that APRA has determined has comparable prudential regulation
- have a credit rating at or above a long-term credit rating of A- (Standard and Poor's) or A3 (Moody's).

EPA retains a right of review if there is a change in ownership or credit standing of the issuing bank or if a concentration risk arises with anyone issuing bank.

Appendix A contains the template EPA needs banks to complete for bank guarantees. Please also note that each of the four major banks has a template on file for financial assurances required by EPA Victoria.

### When it is used

Bank guarantees are commonly used by EPA for quantifiable costs that could pass to the state if a site is abandoned by its duty holder.

## Mutual fund

A mutual fund is a fund created by or on behalf of multiple entities and provides cover to pay out in the event of specific, named events.

Mutual funds:

- are established by agreement between parties
- allow the costs of addressing risk to be shared
- may accumulate to allow increased coverage of a cleanup event compared to single financial assurances from individual duty holders.

### How it works

The combined capital of the mutual fund is usually invested by a professional fund manager, with funds used to meet claims by the members of the fund. The fund manager will need to be approved by EPA.

EPA may consider entering into a separate agreement with the overall manager of the fund or, in some instances, it may become a party to the fund deed.

The amount of the fund is approved by EPA following its consideration of the risk profiles of the entities, the potential size of any claims, whether insurance is held, and the duration of the fund. The fund manager will have to notify EPA of any material issues arising that relate to the fund.

The documents that are executed to establish the mutual fund arrangement are:

- **Fund deed:** The mutual fund is established using a fund deed that sets out who has overall management of the fund, how contributions are to be made to the fund and how claims on the fund are determined.
- **Investment agreement:** An agreement about investment of the funds is also established between the overall manager of the fund and a professional funds manager.
- **Shareholder's agreement:** Where the member entities form a company or trust to have overall responsibility for the fund, a shareholder's agreement or trust deed is also established.
- **Insurance contract:** Insurance protects the fund from large, unexpected claims or an unexpected aggregation of claims.

### When it is used

A mutual fund is appropriate where the member entities have similar obligations and the costs that the fund addresses are contingent in nature rather than known,

required expenditure.

Duty holders will need to seek legal and tax advice on the structure and establishment of a mutual fund. The establishment of a mutual fund may give rise to further responsibilities under other legislation, for example, the Corporations Act 2001 (Cwlth), Insurance Contracts Act 1984 (Cwlth), Insurance Act 1973 (Cwlth) and the Financial Sector (Collection of Data) Act 2001 (Cwlth). It may be that the cost of meeting these regulatory requirements outweighs the benefits of using this type of financial assurance.

EPA will require evidence of processes to ensure that obligations under all relevant state and Commonwealth legislation are complied with.

Duty holders must meet EPA's fees, duties or legal costs on an indemnity basis associated with establishment and maintenance of the fund.

EPA is most likely to accept mutual funds as a form of financial assurance when proposed by an industry association.

## Accumulating third party trust fund

An accumulating trust fund is a fund on behalf of a single duty holder with a third party acting as trustee.

In an accumulating trust fund:

- the trustee is permitted to accumulate income from funds invested in the trust; and/or
- the accumulated income may be added to the capital.

### How it works

An accumulating trust fund is established by a third party approved by EPA to hold cash or other assets on behalf of the duty holder. An example of a suitable third party is an industry association or representative body. A solicitor acting on behalf of the duty holder is not an acceptable third party.

The powers of the trustee and the rights of beneficiaries are set out in the trust agreement. EPA would be a contingent beneficiary of the trust. EPA would register a security interest in the fund under the Personal Property Securities Act 2009 (Cwlth).

The trust can be designed to accumulate a balance over time, or to maintain a constant balance.

The balance of the fund must be regularly reported to EPA by the trustee.

### When it is used

An accumulating trust fund is appropriate for financial assurances needed for long-term operations.

Similar to mutual funds, the establishment of an accumulating trust fund may give rise to further responsibilities under other legislation. Duty holders will need to seek legal and tax advice on the structure and establishment of an accumulating trust fund. It may be that the cost of meeting these regulatory requirements outweighs the benefits of using this type of financial assurance.

EPA will require evidence of processes to ensure that obligations under all relevant state and Commonwealth legislation are complied with.

Duty holders must meet EPA's fees, duties or legal costs on an indemnity basis associated with establishment of the trust agreement, registering a security interest and any other aspects of setup or maintenance of the fund.

### Letter of credit

A letter of credit is an undertaking issued by a bank authorising the payment of money up to a maximum amount according to conditions expressed in the letter of credit to a named person, when that person presents those complying documents to the bank.

In a letter of credit:

- a maximum amount for payment is specified
- the terms under which the letter of credit is claimed are clearly specified.

### How it works

The letter of credit is established in a similar manner to a bank guarantee.

In order to claim against the letter of credit, EPA presents the bank with documentation showing a default on behalf of the duty holder.

### When it is used

Letters of credit are similar to bank guarantees and are appropriate for quantifiable costs that could pass to the state if a site is abandoned by its duty holder.

As letters of credit require EPA to demonstrate the duty holder's default to the bank, letters of credit will only be considered where the risk of the duty holder defaulting on their obligations can be demonstrated to be very low.

Letters of credit can also be used as assurance against default on another type of financial assurance such as payment into an accumulating trust fund.

### Security over land (certificate of title)

A security over land involves EPA securing an interest in a property held by the duty holder or by an associated party.

A security over land would be considered for:

- duty holders who are asset-rich but cash-poor to satisfy financial assurance requirements.

### How it works

An estimate of the value of the land is obtained through the Valuer-General Victoria with instructions from EPA. Other valuations may be considered if they are specifically addressed to EPA and are provided by the valuer to the EPA to allow the EPA to consider the value of a security over the land. However, if EPA considers the valuation is unsatisfactory, EPA will require an additional estimate of value through the Valuer-General. A second estimate may be required where the value of the land exceeds \$750,000.

The value of any business operated on the property is not considered in the estimate of value. It is not expected that the estimate of value considers the cost of any rehabilitation or remediation of the site; however, where there is likely to be rehabilitation or remediation required the value of the land must exceed these anticipated costs, and there must be a high degree of certainty about the extent of contamination at the site. Any other interests on the property such as mortgages or leases must be disclosed to EPA.

An agreement is drafted between the duty holder and EPA which creates an equitable charge on the land that is supported by registration of a caveat. The agreement will include a requirement to execute a mortgage over the title and to appoint the CEO of EPA (or other delegate as the EPA may require) as the attorney of the land owner to execute the charge. If the land offered as security is from a party other than the duty holder, the land holder will be required to enter into a guarantee prepared by EPA.

The mortgage will be in the form prepared by EPA.

The duty holder must meet the costs of the Valuer-General in undertaking the estimate of value as well as any fees, EPA's legal costs on an indemnity basis and duties associated with creating and registering a caveat, the creation and registration of the mortgage and enforcement of the equitable charge and mortgage. If such fees, costs and charges are not paid, interest will be payable at the rate set by the *Penalty Interest Rate Act 1983* (Vic).

## When it is used

A security over land may be considered by EPA as an acceptable type of financial assurance, where the secured value of the land exceeds the amount of financial assurance it is intended to cover. EPA is unlikely to accept the premises on which the business is conducted as security for landfills. EPA may consider security over land that is separate to the premises that is required to provide the financial assurance.

## Contract performance bond

A contract performance bond is an unconditional and irrevocable undertaking issued by a contract bond provider.

It is payable on demand and is worded in a similar way to a bank guarantee.

Contract performance bonds are also known as surety bonds, insurance bonds and unconditional undertakings.

## How it works

Any issuer of a contract performance bond must:

- be regulated by APRA or be based in a country that APRA has determined has comparable prudential regulation
- have a credit rating at or above a long-term credit rating of A- (Standard and Poor's) or A3 (Moody's).

## When it is used

Contract performance bonds are used in the same way as bank guarantees.

## Insurance

Insurance is an indemnity between an insurer and the insured in exchange for premium payments.

Under insurance:

- the insurer has a vested interest in ensuring that the duty holder minimises the risk of a claim
- a wide range of events can be covered, such as third-party damages.

## How it works

An insurance contract is agreed between the parties which sets out the event or events that trigger a pay-out up to a nominated sum to the insured or a nominated party. The contract or policy wording sets out the conditions for payment.

A certificate of currency is issued by the insurer upon acceptance of coverage.

The risks associated with the named events are transferred to the insurer.

EPA may be named as a party with an insurable interest and can then recover cleanup costs directly from the insurer.

## When it is used

Holding insurance for sudden and accidental events and gradual pollution is prudent for any duty holder; this applies to a range of duty holders beyond those that are required to provide financial assurance.

Insurance is not generally available for anticipated costs such as landfill rehabilitation or disposal of stockpiles of waste, which are required to be addressed under financial assurance requirements.

Appendix A – Bank guarantee template

[Letterhead of Bank]

## **Bank Guarantee [Insert ID number of Bank Guarantee]**

### **Recitals**

1. The Financial Institution specified in Item 1 of Schedule 1 (**Bank**) has agreed at the request of the party specified in Item 3 of Schedule 1 (**Guaranteed Party**) to issue this bank guarantee in favour of the party specified in Item 4 of Schedule 1 (**Beneficiary**).
2. This bank guarantee relates to the particulars described in Item 6 of Schedule 1.

### **Operative Part**

The Bank agrees with the Beneficiary as follows:

1. In accordance with this guarantee, the Bank undertakes to unconditionally pay the Beneficiary upon presentation of the original signed guarantee and the completed and original signed form in Schedule 2, any sum or sums, in Australian currency only, up to a maximum of the amount specified in Item 5 of Schedule 1 (**Maximum Amount**).
2.
  - (a) The Bank agrees to make the payment without reference to the Guaranteed Party and notwithstanding any notice from the Guaranteed Party not to pay the Beneficiary any money under this guarantee.
  - (b) Where a demand or payment is made pursuant to this clause 2, for a sum that is less than the Maximum Amount, the Bank may issue (where applicable) to the Beneficiary a replacement guarantee for the balance of the Maximum Amount then remaining, after such part payment or payments, or will return the original guarantee to the Beneficiary.
3. The liability of the Bank under this guarantee will not be discharged or affected because:
  - (a) any of the Guaranteed Party's obligations are varied; or
  - (b) any breach (wilful or otherwise) of its obligations are committed by or on behalf of the Guaranteed Party (with or without the knowledge or consent of the Beneficiary); or
  - (c) the Beneficiary grants any time, credit or concession to the Guaranteed Party or others who have contracted with the Guaranteed Party.
4. This guarantee continues in force until:
  - (a) the Bank pays the Beneficiary the full amount payable under this guarantee, or
  - (b) the Beneficiary notifies the Bank in writing that this guarantee is no longer required, or
  - (c) the time at which the total of all payment of such amounts as the Beneficiary may demand from time to time when aggregated equal the Maximum Amount, or
  - (d) the Guaranteed Party delivers a replacement financial assurance on the same terms as this instrument from a financier acceptable to the Beneficiary in its absolute discretion and for an amount no less than the Maximum Amount.
5. The Bank may pay the Maximum Amount payable to the Beneficiary at any time (less any amounts already paid) and the Bank's liability under this guarantee immediately ceases.
6. The benefit of this instrument is not assignable except that a statutory successor of the Beneficiary will have the same rights as the Beneficiary specified in this undertaking.
7. If this instrument is executed by an attorney of the Bank, the attorney warrants by their execution of this instrument that their power of attorney confers the power to execute this instrument and the appointment has not been revoked.
8. This undertaking is governed by the laws of Victoria.

Dated at:

Signed for and on behalf of  
[insert name of Bank]  
by

in the presence of:

.....  
NAME: [please print]  
POSITION:

.....  
NAME: [please print]

**Schedule 1**

- Item 1 – [INSERT financial institution name]  
[INSERT ABN No.] of the address specified in Item 2
- Item 2 – [INSERT street address of financial institution name]
- Item 3 – [INSERT name of duty holder and its ABN or ACN]
- Item 4 – Environment Protection Authority Victoria ABN 85 899 617 894
- Item 5 – [INSERT A\$ amount of bank guarantee and in words]
- Item 6 – [insert registered business address of duty holder]  
[insert premises address (the land which is subject to the relevant licence/works approval/remedial notice) including lot number and plan]  
[insert number and date of relevant licence/works approval/remedial notice as issued under the *Environment Protection Act 1970*]

**Schedule 2**

(form of demand – Clause 1 of bank guarantee)

TO: [Insert name of Bank]

This is a demand under the Bank Guarantee specified in Item 1 below issued by you on the date specified in Item 2 below. Please pay to the party specified in Item 3 below in immediately available funds the amount specified in Item 4 below. The original signed bank guarantee is **enclosed**.

The person signing this demand confirms that they are authorised and empowered to issue this demand.

- Item 1: Bank Guarantee [Insert ID number of Bank Guarantee]
- Item 2: dd/mm/yyyy
- Item 3: Environment Protection Authority Victoria ABN 85 899 617 894
- Item 4: \$ - not to exceed maximum amount

Dated this                      day of                      year

Signed for and on behalf of the Environment Protection Authority Victoria in the presence of:

Signature of witness:.....                      Signature of authorised person: .....

Name of witness: (print) .....                      Name of authorised person: .....  
Position of authorised person