The following article, written by Jeff Andrilenas, Environmental Lead of the TBLS Group, LLC, in collaboration with Jerome Devillers, CPA and Partner at Mazars USA, appeared in the Summer 2018 edition of The Business Advisor, *a quarterly publication of the Financial Restructuring & Creditors' Rights (FRCR) Department of Gibbons P.C. The article also features an introduction by Natasha Songonuga, a Director in the Gibbons FRCR Department based in the firm's Wilmington, DE office.*

Ms. Songonuga focuses her legal practice on business reorganization and restructuring matters, working across the full spectrum of chapter 11 cases, as well as counseling creditors in assignments for the benefit of creditors state court insolvency proceedings. She is listed in the 2018 Chambers USA Guide to America's Leading Lawyers for Business, *in the Bankruptcy/Restructuring category.*

FINANCIAL RESTRUCTURING & CREDITORS' RIGHTS NEWS

The Business Advisor - Summer 2018

Introduction to Our Guest Article

By: Natasha Songonuga

This edition of *The Business Advisor* features a guest article by Jeff Andrilenas, Executive Vice President and Environmental Lead at The TBLS Group, a transaction-focused environmental valuation advisory firm in New York and New Jersey, and Jerome Devillers, CPA and Partner at Mazars USA, a global accounting firm.

Mr. Andrilenas' and Mr. Devillers' article is entitled **"The Game-Changing Impacts of Revised and New ASTM Standards for Environmental Liability Valuation, Recognition and Disclosure."** Gibbons and TBLS collaborated and presented a game-changer panel on the New ASTM Standards and the potential bankruptcy impact in April 2018, to members of the Commerce and Industry Association of New Jersey.

In the article, the authors discuss the 2017 revisions made to the ASTM International Standards, which are designed to help businesses assess and manage environmental risks and estimate costs and liabilities for environmental matters. The revised standards were developed to reflect certain current best practices in that they now require, among other things, that reporting entities measure estimated environmental liabilities using a fair valuation standard.

Industry-wide adoption of the ASTM's fair market valuation standards, and, in particular, revised standard E2137 (which addresses estimation of environmental liabilities), bodes well for financial market participants, including lenders and investors, as it requires more accurate reporting and valuation standards over the prior "Expected Value Methodology," which should provide a clear understanding of the financial health and risks of businesses with potential environmental liabilities. However, as these revised standards become the industry norms, one should expect an increase not only in valuation disputes but also an increase in the volume of regulatory and investor/lender/creditor litigations, including litigation relating to the use of such revised standards and inadequate valuation of environmental liabilities.

In the bankruptcy context, such increased litigation may likely surface in breach of fiduciary duty claims and investor fraud actions against officers and directors involving allegations assert that a bankrupt entity failed to provide adequate disclosure of its environmental risks or failed to accurately estimate environmental liabilities and provide sufficient reserves pre-bankruptcy in compliance with the fair market valuation under the revised ASTM standards. Increased litigation may also result from the use of a debtor's pre-bankruptcy fair market value estimate. You may see such estimate used as a shield by the debtor in its negotiation with governmental entities, such as the EPA, as the maximum potential liability of the debtor's contingent environmental liabilities, or as a sword by creditors where the pre-bankruptcy valuation showed the debtor to be insolvent, triggering a duty to creditors by management upon such discovery, which may lead to additional fraudulent transfer claims and/or breach of fiduciary duty claims.

Bankruptcy practitioners, whether representing debtors with environmental liabilities or creditors in such bankruptcies, should familiarize themselves with the ASTM standards and the potential risks to (i) management, accountants, and appraisers in a future bankruptcy case if the revised fair market valuation standards are not followed pre-bankruptcy; and (ii) the debtor, if pre-bankruptcy valuation is used against the debtor to set liability in a subsequent bankruptcy estimation proceeding.

We are pleased to have The TBLS Group and Mazars USA as guest authors this quarter.

THE GAME-CHANGING IMPACTS OF REVISED AND NEW ASTM STANDARDS FOR ENVIRONMENTAL LIABILITY VALUATION, RECOGNITION, AND DISCLOSURE

August 2018
The Business Advisor

By: Jeff Andrilenas, Environmental Lead of the TBLS Group, LLC in collaboration with Jerome Devillers, CPA and Partner at Mazars USA

After conducting a major initiative to provide more consistent and comprehensive guidance to environmental professionals relating to the estimation and management of environmental matters, ASTM International has revised two technical standards on the **Disclosure of Environmental Liabilities** (E2173-16) and **Estimating Monetary Costs and Liabilities for Environmental Matters** (E2137-17), and has added a new standard for Recognition and Derecognition of Environmental Liabilities (E3123-17). The changes are designed to mesh ASTM's guidance with existing Generally Accepted Accounting Principles (GAAP) and other accounting requirements companies consider when making decisions relating to the evaluation, recognition, and reporting of environmental liabilities. Clients and their advisors, including environmental, engineering, accounting, and auditing professionals, as well as legal counsel, should familiarize themselves with the requirements of these new standards, because, like GAAP, these standards inevitably will become the commonly accepted ways of estimating and managing environmental obligations.

Change in Approach: Achieve Consistency with GAAP and Other Rules

More Consistent Regime for Disclosures – The biggest underlying change impacting environmental practices is reflected in the revised **E2173-16** Standard Guide, which states that, as of its publication (in November 2016), the guide "is consistent with" GAAP as well as related requirements of the Governmental Accounting Standards Board (GASB), Public Company Accounting Oversight Board (PCAOB), Securities and Exchange Commission (SEC), and Federal Accounting Standards Advisory Board (FASAB). The Guide further states that it is also intended to be consistent with other issuers of accounting standards, including the International Accounting Standards Board (IASB). Formerly, ASTM's approach did not harmonize ASTM guidance on environmental liability disclosures with the accounting protocols governing audited and unaudited financial statements.

Improved Guidance for Estimating Costs – The revised **E2137-17** Standard Guide furnishes a uniform framework for good commercial and customary practice in identifying and estimating costs and liabilities for environmental matters. Estimators of costs and liabilities using this Guide now work within an ASTM context that recognizes FASB, GASB, PCAOB, SEC, FASAB, and IASB requirements. The Guide also contains improved guidance on estimation methods and uncertainty analysis.

New Guide for Recognition/Derecognition – The new ASTM **E3123-17** Standard Guide on recognition and derecognition of environmental liabilities provides an approach for reliably determining whether an environmental liability (a) exists and (b) has subsequently been settled. This Standard Guide confirms use of FASB, GASB, and IASB protocols relating to "Fair Value" and "Probable and Reasonably Estimable" in the valuing of five defined categories of environmental liabilities.

Specifically, the revised and new standards present two general approaches for estimating environmental costs:

- "Fair Value" measurement applies to Asset Retirement Obligations, Environmental Obligations, Commitments, and Guarantees. It is the estimated price that could be received for an asset or paid to settle a liability between knowledgeable marketplace participants. This measurement is a new approach that has been incorporated into the revised standards by the ASTM Subcommittee.

- "Probable and Reasonably Estimable" applies to Environmental Obligations and Contingencies. The "probable" component deals with the probability or likelihood of occurrence. The "reasonably estimable" component is defined according to different accounting protocols. This "probable and reasonably estimable" valuation approach was present in the ASTM standards prior to the present revisions. The new wrinkle (which had not previously been included) is that an environmental liability is required to be valued if it is more likely than not to occur and may be estimated in a range.

Based on these approaches, the new reality is that environmental liabilities are being held to the same GAAP and other accounting standards as other balance sheet liabilities. This shift institutes a regime that varies greatly from requirements and practices under the former ASTM valuation and disclosure standards. The new regime promotes better estimation of environmental liabilities, which is a necessary component of more accurate book and other valuations of companies and enterprises. As such, the ASTM, with its achievement of consistency with GAAP and other accounting statements, rules, and regulations through these new standards, has in effect "codified" a new set of best practices that will have a lasting impact on how companies estimate, recognize, and report environmental liabilities.

For environmental professionals, the revised and new standards create opportunities for more strategic and effective handling of environmental liabilities, including:

- **Financial Planning –** Formulating corporate strategies for addressing environmental liability issues, including book vs. market value "gaps" and timing risks relating to liabilities.

- **Discharging and Reducing Liabilities –** Determining whether Asset Retirement Obligations (AROs) and environmental expenditures are spending at the right levels to discharge the related environmental liabilities and to optimize cash flows, and whether environmental liability spending is being matched by reductions of those liabilities.

- **Cost Allocations –** Mitigating investor and shareholder concerns by managing closure and post-closure environmental liability cost allocations.

- **Divestiture Solutions –** Forming a "valuation" foundation for generating proactive divestiture strategies and solutions for brownfields and environmental liability buyouts.

- **M&A and Real Estate –** Packaging and negotiating environmental liabilities relating to proposed M&A and real estate transactions.

- **Litigation –** Using valuation as a bridge to settle litigation in a recent Natural Resource Damage (NRD) case, use of a valuation prepared under the revised E2137-17 Standard Guide broke an eleven-year impasse and led to settlement.

- **Insurance Assets –** Establishing the value and quality of environmental insurance policies, which can significantly impact pricing of sale/acquisition transactions and reserve calculations.

- **Bankruptcy Proceedings –** Developing pre- and post-petition estimations of environmental liabilities following the revised **E2137-17** Standard Guide.

Conclusion

The ASTM Subcommittee's extensive study of 10-K and 20-F reports served as a catalyst for an unprecedented number of revisions to two existing ASTM standards, as well as the introduction of a new one. The revised **E-2173-16** and **E2137-17** Standard Guides achieve conformity with GAAP and other accounting protocols and, within this improved structure, provide greater guidance and consistency for the valuation and disclosure of environmental liabilities. The new **E3123-17** Standard Guide also conforms to accounting protocols and creates a reliable method for determining whether an environmental liability should be recognized or derecognized. These revisions and new standards are placing environmental liabilities under the same scrutiny as other financial liabilities, with the new framework constituting at once a more comprehensive, as well as a more systematic and granular, approach.

About the Authors

Jeff Andrilenas, PG, LG, LEG is Executive Vice President and Environmental Lead at The TBLS Group. Mr. Andrilenas serves as a member of Subcommittee E50.05 of ASTM International and is responsible with other industry experts for writing and revising ASTM standards relating to environmental risk management. This article was prepared in collaboration with **Jerome Devillers,** CPA and Partner at Mazars USA, **Frances Schlosstein,** President and CEO of The TBLS Group, and **Kenneth B. Furry, Esq.** as counsel to the TBLS Group.

Further Information

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