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**RE: Bank Practitioner Comments on the Proposed Revisions to the California Mitigation Bank Enabling Instrument (BEI) Template**

Ms. Shively:

The California Ecological Restoration Business Association (CalERBA) appreciates the opportunity to provide comments on the revised mitigation Bank Enabling Instrument (BEI) Template to the U.S. Army Corps of Engineers South Pacific Division (USACE) and peer agencies, including the U.S. Fish and Wildlife Service (USFWS), California Department of Fish and Wildlife (CDFW), California Natural Resources Agency (CNRA), the National Marine Fisheries Service (NMFS), the U.S. Environmental Protection Agency (EPA), the State Water Resources Control Board (State Water Board), and the Natural Resources Conservation Service (NRCS) (collectively, the “Agencies”).

CalERBA represents California’s growing ecological restoration industry of companies in the business of land stewardship and delivering wetland, stream, and species mitigation projects. Member businesses support job creation in rural regions and bolster the state’s natural infrastructure through accountable resiliency and biodiversity project outcomes. CalERBA’s members have decades of experience working with the Agencies under mitigation agreements, including the current and prior versions of the BEI template. CalERBA strongly supports the consistency and predictability that mitigation templates provide practitioners to better understand and anticipate mitigation project requirements. We appreciate your leadership and the work of the Agencies to revise the 2021 BEI template to address concerns raised by the banking community, including CalERBA, on the role of the performance security and corresponding requirements. In particular, we appreciate the several opportunities over 2021 and 2022 to confer on our concerns and submit supplemental written feedback on potential solutions. We are pleased to see the Agencies’ efforts to address our concerns in the latest proposed BEI revisions.

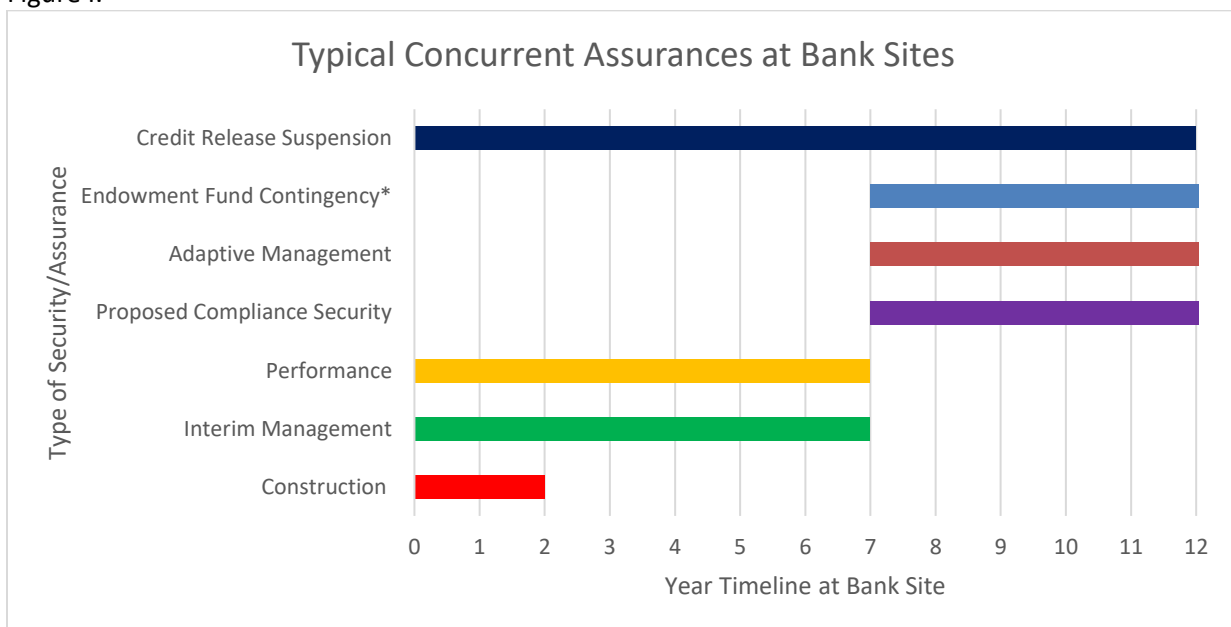
While we agree the proposed BEI revisions are an improvement on the 2021 BEI template, we have several recommendations to better match the newly proposed compliance security with the risk present during its term and improve the BEI review process to incentivize investment in more banks. Notably, we recommend i) revising the defined amount of the Compliance Security, ii) clarifying the scope of Remedial Actions, and iii) expanding the list of permissible financial assurances to include approved bond and insurance forms, which are detailed in Part I below, and a few other comments on the impact of certain proposed revisions and the review process for bankers using the BEI template, covered in Part II.

## Part I

CalERBA appreciates the Agencies' proposal of a Compliance Security to address our concerns with the current BEI's approach of holding the Performance Security through bank closure versus release upon achievement of performance standards. However, the Compliance Security proposal still leaves mitigation bank sponsors exposed to a risk of financial uncertainty because the time for application of advance credits to a permit action, and then closure of the bank, is out of the control of the bank sponsor. This means the Compliance Security may be posted and not returned to the sponsor for twenty or thirty years – all time that the sponsor could have applied the funds backing the security to investment in new and needed successful mitigation bank projects. We hope to work with the Agencies and CalTrans on a solution to this uncertain sunset and return of the security.

We recommend balancing the need for the Compliance Security with the several other risk reduction tools that the Agencies have available in the event of a performance challenge: adaptive management measures, task prioritization, credit release suspension, and endowment contingency funds already in place (these are visually shown below in Figure I).

Figure I.<sup>1</sup>



Generally, we recommend that any material revisions to the BEI template and bank requirements be informed by experiences from the field that reflect the current state of risk at bank sites. From our prior discussions with the Agencies the perceived risk motivating the requirement for an additional security is not supported by recent bank performance data. Stray incidents at permittee-responsible mitigation sites and banks developed prior to the 2008 Compensatory Mitigation Rule (2008 Rule) are not reflective of

<sup>1</sup> Consider that the endowment contingency could be used day 1 of long-term management to fund remedial actions to maintain performance standards after they are initially met or otherwise address reasonably foreseeable adverse impacts. Beyond these overlapping available securities, regulators and bank sponsors can also use adaptive management planning, monitoring reports, and suspension of credit sales (shown through bank closure on the graph) to manage risk and implement corrective action at bank sites.

the maturity and high standards currently common of mitigation banks and their experienced sponsors, especially now that we are collectively over a decade and a half from the Rule's passage. Without fully understanding the risk the Agencies are trying to secure against, it is difficult to collaborate on the appropriate security solution.

After a few years operating under the next iteration of the BEI, we urge the Agencies to revisit the utility of the Compliance Security based on an assessment of how often, if it at all, it was called upon at bank sites and if the Compliance Security was the only solution to remedy the performance challenges or if other tools were also suitable. If the Compliance Security is rarely called upon to play a unique role in performance correction, then we urge the Agencies to eliminate this additional security requirement. We look forward to the opportunity for those discussions and staying in a dialogue on risk assessment at bank sites.

Assuming that the Agencies move forward with finalizing some version of the proposed Compliance Security, we recommend the following changes:

**i. Recommend alternatives to the proposed amount for the Compliance Security**

CalERBA is concerned that the current definition proposed for the Compliance Security as the greater of "10% of the Construction Security or the total estimated costs of foreseeable Remedial Actions" i) represents a security larger than necessary for the performance risks foreseeable at that time and ii) does not provide bankers certainty on which formulation will be required at their bank site.

Regarding this first issue, based on CalERBA members' experience with the risks present during the time between performance achievement and bank closure, 10% of the Construction Security would often tie up more capital than necessary to cover the type of adaptive and remedial actions that occur post-performance achievement. We suggest instead looking at cost estimates for one to two years of long-term management, which is already designed to cover the occasional corrective action following weather events, human trespass, etc. Indeed, the long-term management endowment funds may be a better fit to address actions during this time period than a separate Compliance Security. Already at existing banks long-term management endowment funds may be drawn upon as needed once performance standards are met while still selling credits from the bank. This approach is also supported by the 2008 Rule. At 33 CFR 332.2(n)(4) the Rule states that "Financial assurances *shall be* phased out once the compensatory mitigation project has been determined by the district engineer to be successful in accordance with its performance standards." The Rule's directive supports a reduction in securities and transition to the endowment funding to handle long-term management events as the risk of remediation decreases as the bank nears closure.

Regarding the second issue, we understand that the reference to the option of "foreseeable Remedial Actions" was added in response to a concern that not all banks have a Construction Security. To give sponsors certainty on which option will apply, the Agencies should consider revising to define the Compliance Security as "no greater than 10% of the Construction Security, or for preservation banks lacking a Construction Security, then the total estimated costs of reasonable foreseeable Remedial Actions."

We urge the Agencies to consider the alternative approaches outlined here, but if the Agencies do retain the current definition for the Compliance Security amount, we recommend at a minimum revising the language from the "greater" of the two options to the "lesser" of the two options. By switching to "lesser

than” sponsors will have assurance on the maximum financial commitment the security could represent, i.e. 10% of the Construction Security, but also the option to demonstrate that less than that amount would sufficiently cover potential remedial actions for their particular bank site and proposed restoration objectives.

**ii. Clarify the Scope of Remedial Actions.**

CalERBA recommends more specific language in the template when defining and describing the scope of Remedial Actions that may inform the Compliance Security analysis outlined in the new Exhibit C-5. The current language in Exhibit C-5 of “may include, but are not limited to... adverse impacts... as a result of grading fire breaks during fire control activities, drought, flooding, and human trespass” leaves the analysis required of the sponsor open to speculative events. While the preceding sentence limits to “foreseeable” Remedial Actions, because the actions are all those that “might be necessary through Bank closure,” the language could still result in a subjective back and forth with the sponsor and Agencies over the scope of foreseeable and those actions that “might be necessary.”

We recommend two revisions to clarify the scope of Remedial Actions throughout the BEI. In these revision recommendations we seek to add language that will ensure “foreseeable” Remedial Action discussions between a bank sponsor and the Agencies are based on actual data and adverse events that have occurred at similar bank sites. First, we recommend adding language to the effect of the below in the Exhibit C-5 example description and the definition of Remedial Actions:

*“Remedial Actions are those actions required to resolve a failure to maintain Waters of the U.S., Waters of the State, Covered Species, and Covered Habitat in accordance with the BEI, the Development and Interim Management Plan and Long-term Management Plan either before or after final Performance Standards are met. The suite of Remedial Actions contemplated for each Bank shall be based on reasonably foreseeable events that have occurred on similar landscapes and shall be quantifiable based on past occurrences.”*

Second, to ensure that speculation on events more appropriately characterized as extraordinary circumstances are not brought into the Compliance Security analysis, we recommend adding a sentence either in Exhibit C-5 or the Remedial Action definition that Remedial Actions shall not be misconstrued with Extraordinary Circumstances and their scope shall not be revisited once the BEI is signed.

**iii. Add agency-approved bond and insurance forms as permissible financial assurances.**

Mitigation bankers in the state are currently financially limited in their ability to invest in new mitigation banks due to the few options for short term financial assurances/securities accepted by the Agencies at mitigation bank sites. The restriction to letters of credit hinders bank sponsors by limiting the amount of capital available to be deployed in California for much needed mitigation bank credits. If federal and state agencies could consider other more readily accessible and equally effective financial assurances for California banks, such as surety bonds or insurance, it would enable more bankers to invest in more mitigation banks since a substantial portion of their capital would not be tied up for the operational life of the bank under overlapping letters of credit.

The federal 2008 Compensatory Mitigation Rule (2008 Rule) authorizes the use of four different financial assurance mechanisms for banks: letters of credit (LOC), escrow accounts/cash, surety bonds, and

insurance. A 2011 memo issued by USACE office of Counsel for “all division and district counsel” reiterated that “all forms of financial assurance should be provided an equal opportunity for review and approval if terms can be negotiated that fulfill project-specific requirements.”<sup>2</sup> But California has long treated letters of credit as the exclusively accepted form of financial assurances for mitigation banks. We understand this is in part due to the California Fish and Game Code Section 1798.5(a)(2)(G) specifically calling out that proposed forms of security may be either cash or a LOC. However, the regulation does not state that those may be the only proposed securities, the regulation was promulgated after and influenced by the 2008 Rule with more expansive security options, and California embraces the use of performance bonds to guarantee outcomes in many other prominent and restoration project contexts, including under the Lake and Streambed Alteration program and the Surface Mining Reclamation Act.

CalERBA urges the Agencies to consider revisions to the permissible financial assurances outlined in Section VI(A) of the BEI template to add reference to agency-approved bond and insurance forms. Several insurance and bond companies, including a member of CalERBA, have been working with the Agencies and their offices of counsel to specifically tailor bond and insurance provisions for the unique circumstances of a mitigation bank site, such as the need for Agencies to easily hold and access funds in the event of default or be issued for a multi-year term. As one example of how financial assurances have adapted to the unique needs of bank projects, bonds can now be placed upfront for terms of 10-12 years over a project’s lifespan rather subject to the underwriting uncertainty inherent in annual renewals, guaranteeing extended duration of security. Once a bond or insurance form is vetted by agency counsel, it should be permitted as an option for bank sponsors alongside the historic escrow accounts and LOCs. If the Agencies do not include bonds and insurance in the template language at this point for joint CDFW and peer agency approved banks, at a minimum CalERBA recommends revising the template to allow bonds and insurance if USACE approved at USACE, i.e. 404, mitigation banks so that the template reflects permissible assurances under the 2008 Rule.

Importantly, if these additional financial assurances are not added into the template during this round of BEI revisions, CalERBA urges the Agencies to still agree upon a consistent standard of review for evaluating sponsor requests to use bonds and insurance at a mitigation site. We recommend that the standard is an assessment of whether the proposed alternative assurance is comparable to the functions of a LOC or escrow account, e.g. does the alternative also offer ease of fund access and control in the event of default. This standard based on assessing equivalency across financial assurance forms would also follow the 2011 Memo directive to provide all forms of assurance an “equal opportunity.” The standard should not require that the sponsor demonstrate a special circumstance specific to the resource or bank ecology that warrants the alternative financial assurance. Rather, the standard should center on the financial merits of the assurance. Specifically, we recommend current or foreseeable credit shortfall as a defined circumstance.

## **Part II**

### **i. Timing of Replacement Securities.**

CalERBA has concerns with the release and replacement of securities in the event CDFW or USACE terminates their participation in the BEI. Specifically, new language under Section VIII(E)(1) states that “no security shall be returned until its replacement security is received.” In practice this requirement will place

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<sup>2</sup> *Financial Assurance Instruments for Compensatory Mitigation under the Corps Regulatory Program*, December 1, 2011, HQ U.S. Army Corps of Engineers, Office of Counsel.

an undue burden on the bank sponsor to obtain additional funds to back the letter of credit for the replacement security before they have access to the funds backing the security to be returned. Since it is a result of the agency's decision to terminate, this outcome seems unfair and is yet another support for diversification of accepted financial assurances to include bonds and insurance. It will also particularly challenge smaller banking operations with less flexibility in fund access and potentially increase costs of bank operation for all sponsors who now have to factor in having funds readily on hand for replacement securities.

**ii. Refrain from editing approved BEI template language unless warranted by a unique, specific bank aspect.**

In some regions, CalERBA members experience BEI review delays that result from the Agencies, particularly CDFW and USACE Office of Counsel, proposing revisions to already approved BEI template language. Most often these revisions are unnecessary for bank success and based on the personal interpretation and preference of the reviewing regulator, and not agency guidance or a state specific need. Allowing revisions in this manner leads to inconsistency in mitigation project requirements and causes problematic delays in mitigation implementation. If agency counsel sees a need to start incorporating changes to the BEI template, they should be sharing the template with those revisions in a public notice so the changes are consistently available to all stakeholders and not made in a piecemeal fashion.

We urge the Agencies to embrace the benefits of the BEI template and refrain from editing language previously agreed upon through a transparent, collaborative template development process. The Agencies should only require sponsor changes to template documents when the justification for those changes is grounded in a unique, specific aspect of the subject mitigation bank.

**iii. Thank You and Request to Continue the Conversation on these Recommendations.**

Thank you for your consideration of our industry and these recommendations. CalERBA strongly supports the use of templates by the Agencies and appreciates the Agencies' proposed changes to better facilitate advance mitigation investments. As always, CalERBA is available as an industry resource and welcomes the opportunity to further discuss these specific recommendations and the next version of the template. We are particularly interested in formalizing regular opportunities for discussion between the Project Delivery Team, Banking Agency Management Team, and banking community stakeholders to discuss BEI implementation, challenges the Agencies or bankers may be seeing in the field, and potential future BEI revisions. We look forward to your collaboration.

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