

VALUE ASSURANCE PROGRAMS:
A CASE STUDY IN THE MODEL CITY

May 19, 2011

ABA Tort Trial & Insurance Practice Section
2011 TIPS Annual Spring CLE and Leadership Forum

Speaker:

Jerry M. Dent II, CRE, ASA, FRICS
Managing Director
Alvarez & Marsal Dispute Analysis & Forensic Services, LLC

Authors:

Christina M. McLean, CFA, CRE
Senior Director
Alvarez & Marsal Dispute Analysis & Forensic Services, LLC

Jerry M. Dent II, CRE, ASA, FRICS
Managing Director
Alvarez & Marsal Dispute Analysis & Forensic Services, LLC

ROOTS OF THE MODEL CITY

“Anniston – a remarkable iron-producing, textile-manufacturing, industrial town born in the difficult Reconstruction days and which came to be known far and wide as the ‘Model City’”

“It was a paradigm, the best . . .”

“Anniston still bears the stamp of the careful planning of its founders.”

- Preface to *The Model City of the New South, Anniston, Alabama, 1872-1900*, by Grace Hooten Gates

Founded in 1872 as a private company town, funded by northern investors and fueled by the dreams and ambitions of Samuel Noble and Daniel Tyler, Anniston soon earned its nickname as the “Model City”. From the beginning, the city was designed for industry and the work force that accompanied it. Industry was driven by the abundant iron ore in the region. Much thought and planning was given to community design. Social, religious and educational institutions thrived, and the town flourished.¹

MODERN ANNISTON

Industry continued to boom in Anniston through the first part of the twentieth century, but unfortunately the explosive industrial growth could not be sustained. According to historian Gary Sprayberry,

By the 1980s and 1990s, however, a stagnant economy, a lack of commercial and industrial diversification, the impending closure of Fort McClellan, PCB contamination from the local Monsanto (now Solutia) plant, and the proposed construction of a chemical weapons incinerator at the Anniston Army Depot had left the Model City's economic future in doubt. Many of the factories and mills that had employed thousands and gained the city a reputation for progress and efficiency, such as the Anniston Cordage Company, had been shut down or gutted. A market shift to plastic piping in the 1970s and a general decline in the heavy-metal and concrete industries, as foreign firms became more competitive, further damaged Anniston's economy. By 1993, unemployment rates in the city had inched above 17 percent (Calhoun County's unemployment rate stood at 9 percent). Seven years later, according to the 2000 federal census, the median family income in Anniston stood at \$36,067, far below the national average of \$50,046. More than 20 percent of the city's residents lived below the poverty level.²

The results of Anniston's industrial past have led to “significant contamination problems” according to the United States Environmental Protection Agency³, a multitude of lawsuits⁴, and

¹ *The Model City of the New South, Anniston, Alabama, 1872-1900*, by Grace Hooten Gates, 1978.

² <http://www.encyclopediaofalabama.org/face/Article.jsp?id=h-1464> History of Anniston, by Gary Sprayberry, Columbus State University, updated as of March 8, 2011

³ U.S. EPA Fact Sheet, Anniston PCB Site, Anniston, Calhoun County, Alabama, August 2002.

extensive negative national press⁵, making this a unique environment for any corporate entity defending property value diminution claims in Anniston.

HISTORY OF McWANE, INC.

The origins of McWane, Inc. (“McWane”) can be traced back to Charles Phillip McWane who entered the foundry business in 1871. Through multiple generations and growing through acquisitions and innovations, McWane has transformed from “a modest foundry enterprise” in 1903 to an international operation today with “four pipe facilities, four valve and hydrant facilities, seven soil pipe and utility fittings facilities, seven tank manufacturing facilities and one fire extinguisher facility.”⁶

Two of the company’s acquisitions were located in Anniston. The Union Foundry Company (“Union Foundry”), which produced waterworks fittings, was purchased in 1977. A second plant, M&H Valve Company (“M&H Valve”) was purchased in 1984, allowing the company to diversify into waterworks valves and fire hydrants.⁷

OVERVIEW OF THE ALMON MATTER

The First Amended Class Action Complaint (“Complaint”) in the matter of *Charlie Almon, et al. v. McWane, Inc., et al.* (“Almon”) was filed in December 2004 in the Circuit Court of Calhoun County, Alabama. In it, plaintiffs alleged that McWane, through its ownership and operation of M&H Valve and Union Foundry, caused their properties to be contaminated and their property values to be diminished. Specifically, the Complaint alleges

- 1) Foundry sand (a natural by-product of the foundry operations) containing contaminants such as PCBs, lead, cadmium, zinc, chromium, and arsenic, among others, was given away or sold for residential or commercial fill with no indication it was contaminated;
- 2) Contaminated wastewater was discharged into local sewer systems, creeks and other waterways; and
- 3) Regular emissions were discharged into the air containing lead, soot, foundry sand, particulates and other contaminants.

The proposed class definition included “all property owners, lessees, and licensees of properties on which the defendants’ deposited waste substances, including soot, soil, dust, foundry sand, fluff, PCBs, lead, cadmium, zinc, chromium, arsenic, or other hazardous substances or waste materials, and/or engaged in conduct or practices that allowed such substances and materials to migrate to and/or become located on plaintiffs’ property; . . .” Plaintiffs sought injunctive relief, punitive damages and compensatory damages, along with all other damages to which they may be entitled under Alabama law.

⁴ For example, see *My City Was Gone: One American Town’s Toxic Secret, Its Angry Band of Locals, and a \$700 Million Day in Court*, by Dennis Love, 2006.

⁵ For example, see CBS 60 Minutes: Toxic Town, aired November 2002.

⁶ www.mcwane.com/profile/index.cfm

⁷ www.mcwane.com/profile/pf_timeline.cfm

SETTLEMENT OVERVIEW

The settlement agreement included a Value Assurance Program (“VAP”) to address property value concerns and allowed a satisfactory compromise to be reached. The final settlement agreement included multiple components:

1. Injunctive benefits;
2. Administrative benefits;
3. Cash component; and
4. Value Assurance Program.

The settlement components are described in more detail below.

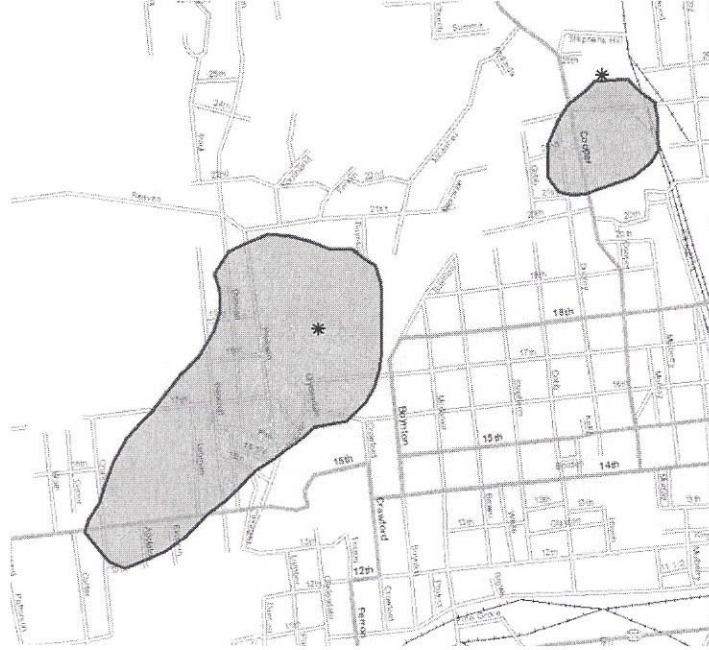
The Final Judgment and Order Approving Settlement and Dismissing Claims (“Final Order”) in the *Almon* matter was entered on March 4, 2010. A preliminary order had been issued in November 2009. Subsequent to the preliminary order being filed and notice being given, owners of only about one-fifth of 1% of the more than 64,000 potential parcels of the settlement class chose to opt-out of the proposed settlement.

In the Final Order, Judge Joel Laird wrote that

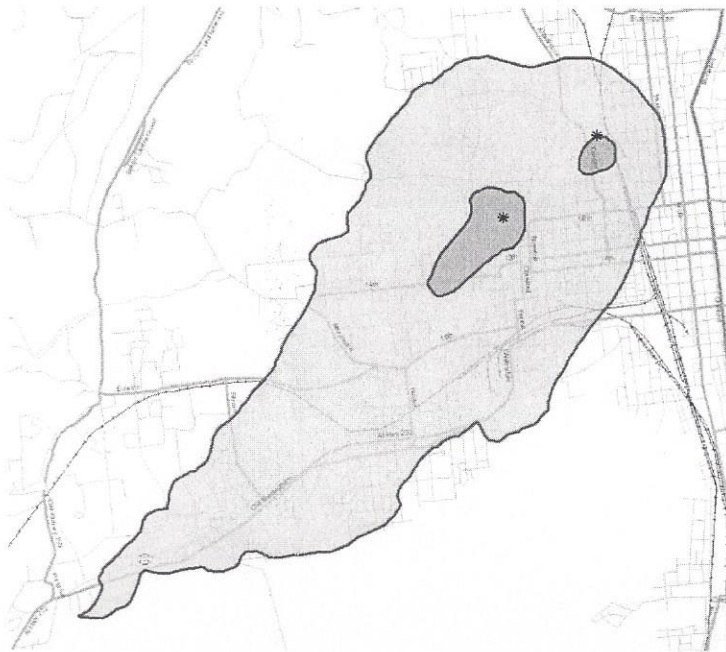
(i) the Settlement provides significant financial benefits to Settlement Class Members; (ii) there is no evidence suggesting that the Settlement was the result of anything other than good-faith arms-length negotiations; (iii) counsel for the Settlement Class conducted a reasonable and thorough investigation of the facts and law relating to the claims asserted by Settlement Class Members . . . ; and (iv) counsel for the Settlement Class are experienced in class action litigation . . . the terms of the settlement . . . are in all respects fair, just, reasonable, and adequate and in the best interests of the plaintiffs and to the Settlement Class.

Through settlement negotiations, three settlement zones were ultimately agreed upon:

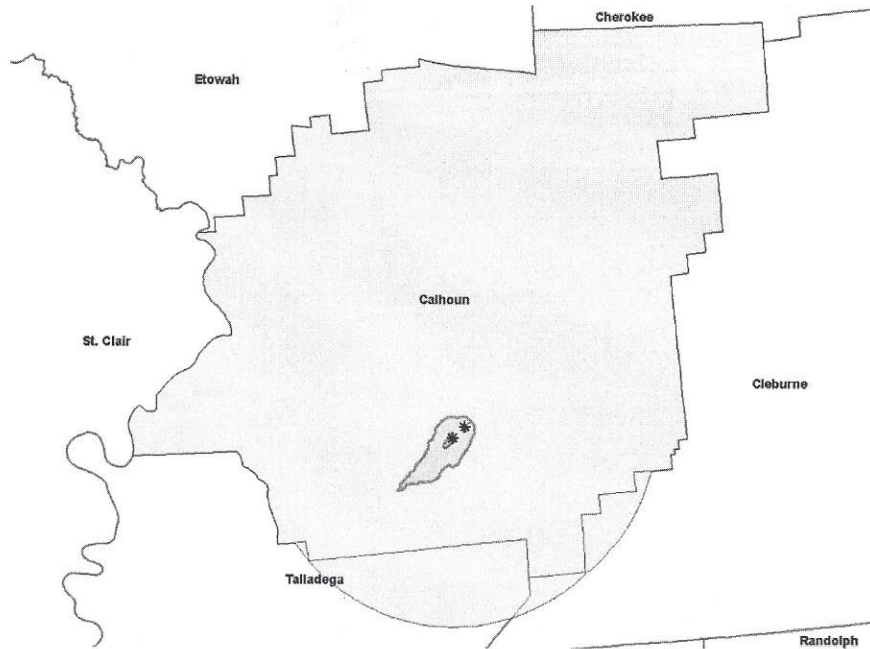
1. **“Settlement Zone A”** – Residential Property located nearest Union Foundry and M&H Valve, excluding the properties that were the subject of a prior settlement (the *Baker Settlement Class*);



2. **“Settlement Zone B”** – Residential Property located from the boundary of Settlement Zone A in all directions to the boundary shown on the map, excluding the properties that were the subject of the *Baker Settlement Class*; and



3. **“Settlement Zone C”** – Residential Property located from the boundary of Settlement Zone B in all directions to the boundary shown on the map. This includes all of Calhoun County, Alabama, and portions of Talladega and Cleburne Counties.



Injunctive Benefits

McWane agreed to no less than \$1 million in site improvements at Union Foundry and M&H Valve to be performed within two years of the effective date of the settlement.

Administrative Benefits

Other than specific exceptions related to the VAP described below, McWane agreed to be responsible for all expenses related to class notice and administration of the settlement, including the costs of the settlement administrator.

Cash Component

McWane agreed to pay \$4.2 million into a fund to be distributed by the settlement administrator in its entirety. The funds must be used to pay incentive rewards to the class representatives, cash claims made by eligible class members, and attorney’s fees and expenses. Any remainder will be distributed to a charity or program agreed upon by all parties and approved by the court.

Value Assurance Program

A VAP is a contract between the VAP sponsor (in this instance, McWane) and eligible participants. Although nearly all aspects of a VAP are flexible and can be customized for a particular site and/or issue, at its core every VAP is a promise to compensate eligible participants if their property should sell for less than market value during a specified timeframe.

A VAP can be a powerful stabilizing force in a residential real estate market that is skittish due to real *or* perceived environmental issues. It calms homeowner fears by protecting the value of what is likely their most valuable asset. It preserves property values and provides liquidity to the market. A VAP builds public trust and opens a line of communication between the sponsor and the community. For the sponsor, a VAP spreads settlement dollars to a larger potential pool of recipients. In a traditional settlement, a payment may be made to every person irrespective of actual documented damage. In a VAP, while the protection is available to every eligible participant, compensation only occurs when damage is actually documented.

As mentioned previously, every aspect of a VAP is customizable (and therefore negotiable as a tool for reaching settlement):

- Structure – timeframe, sub-classes, right of first refusal, required documentation, etc.
- Eligibility – geography, property types, owners, test results, etc.
- Incentives – real estate agent commissions, home improvement grants, etc.
- Provisions – mortgage subsidies, relocation expense reimbursement, environmental insurance policies, etc.

ALMON VAP

Program Eligibility and Definitions

As part of the final settlement, the VAP is a completely voluntary program and is available to current owners as of November 23, 2009, of eligible residential property within the settlement zones.

The VAP is not an offer to purchase property but rather is a means of compensating eligible property owners in the event their property sells for less than fair market value.

Eligibility for the VAP is determined as follows:

- Property must be within one of the Defined Program Areas (i.e., the three settlement zones),
- Property must be Residential Property,
- Property must meet all testing and other requirements as defined in the VAP booklet,
- Property must be owned by an individual and not as part of a business, and
- Sale must occur between April 26, 2010 and April 26, 2013.

In addition, property owners who choose to sell must follow the criteria below:

- Property must be listed with an Approved Real Estate Agent

- Reasonable Efforts to obtain the maximum sale price must be made
- Claim to the VAP must be made within thirty (30) days of closing.

Each of the eligibility criteria and key terms are defined in greater detail in the VAP booklet that was made available to all eligible property owners.

Fair Market Value (“FMV”) is a fundamental concept to the structure of the VAP. As such, it is clearly defined in the VAP booklet as follows:

Fair Market Value is what your property is worth at the time of sale, absent the influence of any real or perceived environmental issues. To determine the value of your property, the VAP Administrator will use established appraisal techniques such as the market-based approach, historical appreciation rates, statistical modeling and/or adjusted assessed values.

Reasonable Efforts are also a key component of the VAP. Reasonable Efforts were thus defined to include:

1. You must list the property with one of the Approved Real Estate Agents. These are agents fully licensed to sell residential property, who are familiar with your neighborhood and who have agreed to participate in the VAP.
2. You must make diligent efforts to comply with the reasonable suggestions of your Approved Real Estate Agent, including listing the property at the appropriate price, making reasonable improvements to your property not to exceed \$1,000, advertising your property and showing your property.
3. The transaction must be arm’s length. This means that if you sell your property to a related party, such as a friend or relative, for less than Fair Market Value you are not eligible to participate in the VAP.

Program participation varies based on the settlement zone in which a property is located. The following matrix identifies the basic requirements and benefits for each zone, which are discussed in greater detail below.

Table 1: Basic Requirements for VAP Participation

Settlement Zone	Qualified Analytical Data	Proof of McWane Foundry Sand
A	Not Required	Not Required
B	Required	Optional
C	Required	Required

Table 2: VAP Restitution Percentage by Zone and Requirement

Settlement Zone	Qualified Analytical Data	Proof of McWane Foundry Sand	Restitution Percentage
A	N/A	N/A	25%
B	Yes	Yes	100%
B	Yes	No	7.5%
B	No	No	0%
C	Yes	Yes	100%
C	Yes	No	0%
C	No	No	0%

Qualified Analytical Data

Properties in Settlement Zones B and C are only eligible for the VAP if they have Qualified Analytical Data. In order to meet the condition of “Qualified Analytical Data”, sampling must be performed by an Approved Environmental Firm (defined within the VAP booklet) and soil results must meet one of the agreed upon thresholds: 1) Lead must be 350 ppm or higher, or 2) Cadmium must be 3.7 ppm or higher and Chromium must be 10,000 ppm or higher.

If sampling was not performed previously by Class Counsel’s consultant, certain procedures must be followed by the VAP participant in order to retain eligibility. Specifically, the property owner must submit

1. New Qualified Analytical Data Request Form (found in the VAP booklet),
2. Access for Testing Form signed by the new owner (because the property will have been sold at this point) for the sampling and analysis to be performed, and
3. \$250 advance payment toward the cost of the sampling and analysis.

Proof of McWane Foundry Sand

In addition, members of Settlement Zone C must provide documentation of the receipt of foundry sand from Union Foundry or M&H Valve during McWane’s period of ownership (1977 to present and 1984 to present, respectively) in order to be eligible for benefits under the VAP. Members of Settlement Zone B, at their discretion, may choose to submit such documentation in order to receive a greater benefit from the VAP than they would otherwise be eligible.

In order to prove receipt of foundry sand, the claimant must provide evidence that 1) the person received foundry sand during the specific periods named and 2) the foundry sand originated from a McWane facility. An independent Special Master will evaluate these claims, either through written documentation, sworn oral testimony, or both, that a property was the recipient of foundry sand from one of the McWane Plants during the time period of ownership and operation.

The VAP participant must do the following to preserve eligibility:

1. Confirm in writing the desire to submit Proof of McWane Foundry Sand,
2. Submit documentation, if any, of receipt of foundry sand from Union Foundry or M&H valve, and
3. Submit \$250 toward the cost of the process (Special Master).

Proof of McWane Foundry Sand will be deemed to exist if one of the following is met:

- Documentation, such as a bill of lading, manifest, receipt of payment, or similar, showing receipt of foundry sand from Union Foundry or M&H Valve during McWane's time period of ownership and operation; or
- Testimony by the claimant and one additional person unrelated to the claimant, submitted under oath (and possibly recorded by a court reporter), based upon personal knowledge, and subject to the penalty of perjury, before the designated Special Master confirming the delivery of foundry sand to the property from Union Foundry or M&H Valve during McWane's time period of ownership and operation. The testimony cannot be hearsay.

VAP Process

Although the requirements vary widely, the basic process for participants in each settlement zone is similar. When the property owner is ready to sell, he or she must list the property with an Approved Real Estate Agent. These agents have been selected as those active and familiar with the area, have received training regarding the VAP and its requirements, and are willing and able to guide participants through the process. The property owner must then follow the agent's suggestions and make Reasonable Efforts to sell the property for the highest amount possible.

When a written offer is received that the property owner desires to accept, the required form is completed and submitted to the VAP Administrator. At that time, McWane will have 48 hours to decide if it would like to purchase the property. McWane, if it chooses to purchase, will pay the offer price or FMV, whichever is greater. If McWane chooses not to purchase, the offer may be accepted and closing occurs in a typical fashion.

After closing, and assuming McWane does not purchase the property, the seller (i.e., the former property owner) may choose to make a claim to the VAP if he or she feels as though the sale price received was less than FMV. Once a claim form is received, the VAP administrator will establish the FMV of the property and compare to sale price.

The remainder of the claims process varies by settlement zone:

Settlement Zone A. No other action is required by the claimant. If FMV is greater than sale price, the seller will be compensated for the difference multiplied by the appropriate restitution percentage. If sale price is greater than FMV, no payment is due from the VAP.

Settlement Zone B. The claimant must also provide Qualified Analytical Data as discussed above. If Qualified Analytical Data is provided, and if FMV is greater than sale price, the seller will be compensated for the difference multiplied by the appropriate restitution percentage (in this case, 7.5%). However, at his or her discretion, the claimant may also provide Proof of McWane Foundry Sand as discussed above. If Proof of McWane Foundry Sand is also provided, and FMV is greater than sale price, the seller will be compensated for 100% of the difference. If sale price is greater than FMV, or if the property does not have Qualified Analytical Data, no payment will be made from the VAP and Proof of McWane Foundry Sand is irrelevant.

Settlement Zone C. The claimant must provide both Qualified Analytical Data and Proof of McWane Foundry Sand. If this requirement is not met, no payment is due from the VAP. If sale price is greater than FMV, no payment is due from the VAP. However, if both criteria are met and sale price is less than FMV, the seller will be compensated for 100% of the difference.

CONCLUSION

Absent health claims, property owners are primarily concerned with protecting the value of their most important (and typically most valuable) asset – their home. A VAP is a direct means to address fears of property value diminution. Analysis of former VAPs has illustrated the stability a VAP provides to the real estate market by returning time on market, average sale price and other real estate metrics to pre-VAP conditions. The *Almon* settlement is an excellent example of a creative approach where property owners benefit because they will be compensated should they sell at less than Fair Market Value and McWane will benefit because only property owners truly damaged will be receive benefits. In the end, all stakeholders benefit from the VAP as the economics of the market returns to ordinary supply and demand conditions.