

Commercial Real Estate Demands An Environmental Risk Policy

Credit Union Journal | Monday, November 26, 2012 Written By: Gary Reynolds, Principal at Partner Engineering and Science, Inc.

As more credit unions venture into the commercial real estate market, having an environmental risk management policy becomes increasingly important for many reasons, including:

- Ensuring the CU is not exposed to environmental liabilities, such as being responsible for the cleanup on a foreclosed contaminated property.
- Avoiding potential losses from not being able to foreclose on a property because it is contaminated.
- Evaluating whether environmental concerns will reduce the value of the property or affect the borrower's ability to repay the loan.
- Avoiding negative PR involved with a contaminated site.

Environmental due diligence is often dictated by where the financing is coming from. Many credit unions are participating in Small Business Administration (SBA) lending, which has specific requirements on what and how environmental investigations are done. Even for non-SBA commercial loans, regulators have stated that lending institutions should have an environmental policy and that all loans adhere to it. The SBA's environmental policy is a great guideline.

The SBA's Environmental Policy?

Lenders participating in SBA 7a and 504 loan products are required to follow the Environmental Investigation requirements in the latest SBA Standard Operating Procedure (SOP) 5010 5 (e). Understanding these requirements will help prevent issues that could delay the loan and sour your borrower.

The SBA's policy is tiered based on Environmentally Sensitive Industries and loan amounts, with the requirements in the SOP representing the minimum amount of environmental due diligence accepted. In the SOP, Appendix 4, SBA has provided the list of Environmentally Sensitive Industries (such as industrial or automotive servicing) by NAICS code.

Lower-Risk Properties

If the property type is not listed on the NAICS list, then the SBA only requires limited environmental screening tools. If the SBA's portion of the loan is UNDER \$150,000 due diligence can start with an Environmental Questionnaire completed by the lender and the owner/occupant. The questionnaire inquires about the property's current and past uses, as well as the adjoining properties, with the intent of identifying environmentally risky operations that may have contaminated the property. If a concern is identified, then the level of due diligence increases to an environmental report – at least a Records Search with Risk Assessment.

If the SBA's portion of the loan is over \$150,000.00 then the lender can start with a Records Search with Risk Assessment or "RSRA" (a desktop environmental report). The RSRA includes a review of government and historical records, the property's NAICS code, and the Environmental Questionnaire, to identify environmentally sensitive operations on the property or nearby. If the RSRA identifies a potential concern, a full Phase I Environmental Site Assessment (ESA) must be done.

Higher-Risk Properties

Any property types/usages (including collateral properties) on the NAICS list of Environmentally Sensitive Industries are required to start the due-diligence process with an AAI Phase I Environmental Site Assessment as defined in ASTM 1527-05. The Phase I ESA is the gold standard for environmental due diligence, and includes a site inspection by a qualified environmental professional or scientist, review of government and historical records, interviews of key personnel, review of area geology and hydrogeology, and other items.

For high-risk facilities (such as dry cleaners and gas stations), the SBA has more requirements above Phase I ESA. Child care centers, nursery schools and residential care facilities occupied by children and constructed before 1980 must undergo a lead risk assessment for paint and testing for lead in water.

Choosing an Environmental Firm

An important consideration for credit unions before engaging a firm for an SBA project is to make sure that the consultant understands and will sign the SBA Reliance Letter without altering it. If they won't sign it, the SBA will screen the report out and require a new report by a firm that will sign the Reliance Letter – causing you to pay twice and delay the closing.

Whether the deal is an SBA loan or not, choosing a firm that's available for questions and can be true a consultant is a great partnership to form – for the credit union and the borrower.

Gary Reynolds is an SBA Specialist and Principal with Partner Engineering & Science, Inc. For info: www.partneresi.com.