



Due Diligence. *Done Simply. Done Right.*



Environmental Due Diligence for SBA Loans

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— ORMS Overview —

National provider of environmental risk management with over 25 years due diligence/risk experience.

- Founded by an environmental risk management professional in 2009; privately owned
- Serve hundreds of lenders (including CDCs and 7A lenders) by providing the tools needed to develop and manage environmental policies and procedures that help close deals quickly
- ORMS serves as an extension of our lender clients
- Members of NAGGL, CT Real Estate Finance Association, RMA, Environmental Bankers Association , NADCO
- Expertise in Lender Due Diligence, SBA
- ORMS was founded with SBA lenders, credit unions, community and regional banks as its primary focus;
- ORMS helps lenders do more risk management in a cost-effective manner by outsourcing the environmental risk management process.

— Key Differentiators

- We serve as lenders' "virtual" environmental risk manager
- We DO NOT do Phase I's, Phase II's or other field work.
- We use the information available to help you make decisions as well as a professional opinion, recommendation and consultation after review.
- ORMS is set up to be a business advisor with our clients, not a product-driven company.
- Extensive national network of environmental professionals

How Environmental “Fits in”



Borrowers'/Loan Officers' Reaction when you tell them they need to do environmental...



The Reaction when they find out there are Environmental Problems...



What the process can feel like...



— SBA Highlights —

- SBA is the only government agency that provides a specific environmental policy
- SBA helps lenders and consultants when possible
- SBA loans have skyrocketed over the past 12 months
- The SBA team is so helpful to the industry



U.S. Small Business
Administration

SBA's Environmental Policies and Procedures

April 29, 2021

Sources of SBA Environmental Policy

- Loan Origination - Environmental Policies and Procedures
 - 7(a)/504 Loans: Pages 215 - 223 of SOP 50 10 6
 - Definitions (Appendix 4)
 - Reliance Letter Template (Appendix 5)
 - List of NAICS Codes of Environmentally Sensitive Industries (Appendix 6)
 - Gas Station Requirements (Appendix 7)
 - SBA Indemnification Agreement (Appendix 8)
- Loan Servicing and Liquidation - Environmental Policies and Procedures
 - 7(a) Loans: Pages 37-45 of SOP 50 57 (2)
 - 504 Loans: Pages 41-49 of SOP 50 55

The SOPs Establish Minimum Requirements and Utilize a Tiered Approach

- SBA requires an Environmental Investigation of all commercial Property that will serve as collateral for an SBA loan.
- Environmental Investigations are not required for residential real estate collateral.
- Tiered Approach: The type and depth of the Environmental Investigation to be performed varies with the risks of Contamination.
- SBA's SOPs establish minimum environmental requirements for the 7(a) and 504 loan programs. Internal Lender and CDC policies may require additional Environmental Investigations or safeguards. Prudent lending practices may also dictate additional Environmental Investigations or safeguards.

Environmental Investigations Recognized by the SOPs

1. Environmental Questionnaire
2. Records Search with Risk Assessment
3. Transaction Screen
4. Phase I
5. Phase II

Environmental Questionnaire

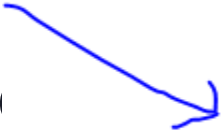
- Just that – A questionnaire used by the lender/CDC to determine the likelihood of contamination at the Property.
- The lender/CDC must make at least one site visit to the Property and the Environmental Questionnaire must inquire into past and present uses of the subject Property and adjoining properties.
 - Specific areas of inquiry that the Environmental Questionnaire must delve into are set forth in the “Definitions” section of the SOP (Appendix 4).
 - Lenders/CDCs may use the Transaction Screen questionnaire (from ASTM E1528-14), which is an excellent template.
 - The current owner (which may be the seller) or the operator of the Property must sign the EQ. If the current owner or operator of the Property will not sign the EQ, an EQ cannot be used. Lender/CDC must, at a minimum, obtain a Transaction Screen.

False Statements Certification


SOP 50 10 6

Appendix 4: Definitions - Environmental

loan. Environmental Questionnaires must be completed or reviewed by a Lender that has made at least one site visit to the Property and a good faith effort to conduct an interview with the current owner or operator of the Property. An Environmental Professional may, but is not required to, assist with the responses to the questionnaire. An Environmental Questionnaire may be considered if it was completed up to 1 year prior to submission. The current owner or operator of the Property must sign the Environmental Questionnaire. If the current owner or operator of the Property will not sign the Environmental Questionnaire it cannot be used and lender must then, at a minimum, obtain a Transaction Screen.



An acceptable Environmental Questionnaire must include, in addition to the required areas of inquiry listed below, the following language with respect to false statements: “The undersigned owner(s) and/or operator(s) acknowledge(s) and agree(s) that intentionally falsifying or concealing any material fact with regard to the subject matter of this Environmental Questionnaire may, in addition to other penalties, result in prosecution under applicable law including 18 U.S.C. section 1001.”



Records Search with Risk Assessment

- Performed by an Environmental Professional.
- Consists of a search of government environmental databases (same databases reviewed for a Phase I) and historical records.
- A determination by the Environmental Professional that the property is “low risk” or “elevated risk” or “high risk” for Contamination.

Transaction Screen

- A limited environmental investigation conducted in accordance with ASTM E1528-14.
- SBA has additional requirements for a Transaction Screen that go beyond industry requirements. SBA requires:
 - The Transaction Screen must be performed by an Environmental Professional
 - Conclusion by Environmental Professional
 - Must be accompanied by SBA's template Reliance Letter

Phase I

- Must be “AAI” compliant (i.e., prepared in accordance with EPA’s regulations for “All Appropriate Inquiries” – An SBA requirement since November 2006)
- A Phase I prepared pursuant to ASTM E1527-13 is “AAI” compliant
- The Environmental Professional must conclude that either:
 - (1) the risk of Contamination at the Property is minimal and no further investigation is warranted, or
 - (2) the risk is sufficient to warrant additional investigation.

(Note: The EP is not required to use this exact phrase but rather may use words to this effect).

Phase II

- Performed by Environmental Professional
- Sampling for contamination in soil and/or groundwater
- Vapor Intrusion Testing (growing recommendation in Phase I's)
- Report stating:
 - Whether Contamination quantities exceed reportable/actionable levels
 - Whether Remediation is necessary
 - An estimate of Remediation costs
 - Any projected completion date for Remediation

Reliance Letter

- All Transaction Screens, Phase I and Phase II reports **must** be accompanied by the SBA's template Reliance Letter that appears in Appendix 5 of SOP 5010 6. The Reliance Letter may not be modified in any respect.
- The Reliance Letter must be addressed to the Lender and to SBA.
- Evidence of the Environmental Professional's Errors & Omissions Liability Insurance with minimum coverage of \$1 million per claim (or occurrence) must be attached to the Reliance Letter. (Lender and SBA do not have to be named insureds or loss payees).
- Lender or SBA may provide Borrower with a copy of the Environmental Investigation *for informational purposes only*.
- Lenders and CDCs are prohibited from entering into any agreements that alter the terms of SBA's standard reliance letter.

Steps of the Environmental Investigation

- **NAICS Codes** – Lenders and CDCs first determine the NAICS codes for the property's *current and known prior uses* and compare them to the list of NAICS codes of environmentally sensitive industries in Appendix 6. If there is a match, then the environmental investigation must begin with a Phase I.

Exception: If the property is a unit in a multi-unit building, lenders and CDCs may begin with an RSRA.

If no NAICS Code match....

- **Loans up to \$250,000** – The investigation may begin with an EQ. If the EQ reveals that contamination is unlikely, this is sufficient.
- **Loans over \$250,000** – The investigation must, at a minimum, begin with an EQ and a RSRA.
 - If the results of the RSRA conclude that the Property is anything other than “**Low Risk**” for contamination, a Phase I must be obtained.

If a Phase I Recommends Additional Environmental Investigation....

- If the lender/CDC still wishes to make the loan, then a Phase II is needed.
- If a Phase II finds no evidence of contamination, that is all that is needed.
- If a Phase II reveals contamination ---

Approval & Disbursement in the Presence of Contamination or Remediation

- SBA may approve a loan or disbursement of a loan even if the property is contaminated or is undergoing remediation. The decision relies upon consideration and application of one or more of the nine mitigating factors identified in the SOP.
- If an SBA lender or CDC has “delegated authority” (PLP lender or PCLP CDC), the lender or CDC will make this determination internally, and document their loan file accordingly.

Section E.6 Write-Up

Lenders and CDCs seeking loan approval or disbursement authority despite Contamination or on-going Remediation at the Property must submit a recommendation to SBA that includes, at a minimum, a discussion of the following:

1. Nature and Extent of the Contamination
2. Remediation
3. Collateral Value
4. Mitigating Factors

Mitigating Factors

- a) Indemnification
- b) Completed Remediation
- c) No Further Action
- d) Minimal Contamination with Minimal Remediation
- e) Clean-up Funds
- f) Escrow Account
- g) Groundwater Contamination Originating from Another Site
- h) Additional or Substitute Collateral
- i) Other Factors

Special Use Facilities – Child-Occupied Facilities

- “Child-Occupied Facilities” constructed prior to 1978 that are visited regularly by the same child under 6 years of age must undergo a lead risk assessment for lead-based paint and lead in the drinking water, and any risk of lead exposure must be sufficiently minimized.

Special Use Facilities - Drycleaners

- On-site dry cleaners which may have utilized tetrachloroethylene (PCE) and trichloroethylene (TCE) and/or petroleum-based solvents in the course of their business operations, may present significant clean-up costs. As such, a Phase I and Phase II are required.
- Vapor Intrusion testing should be conducted if warranted by the circumstances or recommended by the Environmental Professional.

Special Use Facilities – Gas Station Loans

- Environmental Investigation Requirements for Gas Stations are set forth in detail in Appendix 7 and always begin with a Phase I.
- Environmental Investigation results:
 - Property is not contaminated – Submit results to the SBA.
 - Property is contaminated – Lender may either decline the loan or follow the requirements set forth for approval and disbursement of loans when there is contamination and remediation at the property *provided that at a minimum, the SBA Indemnification Agreement must always be obtained and signed by the seller.*

Gas Station Equipment Testing

- SBA requires that the EP to determine whether or not the gas station is in compliance with all state requirements, if any, pertaining to tank and equipment testing and provide documentation of this.
- All leaking or other defective equipment must be replaced or repaired prior to disbursement:
 - Any provision in the purchase and sale agreement that allows the seller to avoid repair (e.g., credit towards the purchase price or a lump sum payment) is not acceptable
- A loan may not be disbursed unless full compliance is achieved.

Appeal Process and Exceptions to Policy

- The SBA has an appeals process.
- Appeals, including exceptions to environmental policy, are reviewed by the Environmental Committee.
- Lenders and CDCs that believe that a decision rendered by SBA is inconsistent with the SOP, or who seek an exception to policy, may appeal to the committee by sending a copy of the decision, supporting documentation and an explanation to EnvironmentalAppeals@sba.gov

Recent Environmental Committee Reviews: The Numbers and Common Requests

- **By the numbers:** 251 total matters (170 appeals, 80 questions answered, and 1 insurance deductible). Average response time: 1.93 days.
- **Common requests for exceptions to policy that we receive:**
 - Use of Phase I reports that are out-of-date (allowed when we can conclude that the risk to the SBA is minimal);
 - Permission for an EP to go directly from a Transaction Screen to a Phase II (granted less often due to the loss of innocent landowner protections afforded through AAI; requires an EP recommendation and more analysis);
 - Consent to perform less environmental due diligence than our written policies require (authorized when we can determine that the risk to SBA is low).

Common Errors on Environmental Submissions to SBA

- Reliance Letters
 - Not using the most current version.
 - Modifications to the letter.
- Section E.6 Factors for Contaminated Properties
 - Not submitting a Section E.6 analysis.
 - Not specifying one of the SOP mitigating factors.
 - Submitting insufficient analysis of the recommended mitigating factor. Please address the criteria listed in the SOP for the specific factor.
 - Leaving out the discussion of collateral value in a Section E.6 analysis.
 - Recommending “Minimal contamination with minimum remediation” as a mitigating factor for properties with a long history of contamination and remediation.

Common Errors on Environmental Submissions to SBA

- Submittal Issues

- Submitting locked or scanned pdf reports that are not searchable.
- Resubmitting previously submitted documents. Please submit only the items requested.
- Submitting a single pdf document that has all the files but does not contain an index for the location of pertinent items like a NFA letter etc.
- Reports that are not dated or do not have a day, .i.e. May 2018 rather than May 15, 2018.

- Miscellaneous

- Conducting vapor sampling without also addressing potential soil and groundwater contamination.
- For child-occupied facilities, not testing all taps, faucets, and fountains likely to be used as a source of drinking water.
- Not including a tank testing compliance statement in a Phase I Assessment for an active gas station.

Sufficient Due Diligence

All Media – Soil, Groundwater, Soil Vapor

- ASTM 1527-13 – Phase I must assess vapor migration
- Increase of Phase II reports that only include soil vapor samples
- Is soil vapor sampling alone sufficient?
- Issue:
 - Pathway analysis: only open pathway is vapor intrusion
 - Potential liability risk from regulatory requirements: high GW concentrations may trigger reporting/remediation requirements, offsite migration

Tips

Vapor Issues

1. Phase I recommends investigation of soil, groundwater and soil vapor, Phase II only includes soil vapor sampling.

- *Tip: Provide a **detailed explanation** in the Phase II why no soil or GW sampling conducted (GW depth, bedrock, prior sampling, etc).*

2. Phase I only recommends soil vapor sampling.

*Tip: Include a **detailed explanation** in the Phase I Assessment why no soil or GW sampling is recommended.*

3. Vague statement regarding liability from groundwater migration from offsite.

Tip: Provide specific reference to local regulations or laws.

How you can help SBA

- If you have an issue or concern with SBA's Environmental Policies and Procedures (or if there is language or a requirement in our loan processing, servicing or liquidation SOPs that just make you crazy), identify it for us and suggest an improvement. We review every suggestion and many the ideas from Environmental Professionals and others have been incorporated into the annual revisions to our policies.
- Suggestions, appeals, requests for exceptions to policy and requests to use "Other Factor(s)" for disbursement in the presence of contamination can be sent to:
EnvironmentalAppeals@sba.gov

— Environmental Best Practices —

- ***Have as much control of the process as possible***
 - *Start the process as early as possible.*
 - *Try not to let borrowers control due diligence when possible.*
 - ***Collect as much information (i.e. all previous Phase I's, Phase II's, UST removal reports, etc.) that is available UP FRONT...reduces the time to get to the "finish line".***
- *Gas stations and dry cleaners sites undergoing remediation WILL take longer to get approval.*
- *Make sure reports are correct*

It's Risk Management



How Much and How Long?

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