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Guaranteed Loan Assistance and Environmental Risk Analysis

This document contains a brief overview of the environmental risk analysis requirement that is associated with the approval of a loan guarantee in order to evaluate real property security for the presence of potential environmental risks such as hazardous waste or underground storage tanks.

This document is intended for information only and does not replace the environmental review or any environmental compliance requirements that must be completed before a loan guarantee can be approved by FSA.

Background on Loan Guarantees

FSA guaranteed loans provide lenders (e.g., banks, Farm Credit System institutions, credit unions) with a guarantee of up to 95 percent of the loss of principal and interest on a loan. Farmers and ranchers apply to an agricultural lender, which then arranges for the guarantee. The FSA guarantee permits lenders to make agricultural credit available to farmers who do not meet the lender's normal underwriting criteria.

FSA guaranteed loans are for both Farm Ownership and Operating purposes. Like the Direct Loan Program, a percentage of Guaranteed Loan funds are targeted to beginning farmers/ranchers and minority applicants.

Loan Purposes

Farm Ownership Loans

Guaranteed Farm Ownership (FO) Loans may be made to purchase farmland, construct or repair buildings and other fixtures, develop farmland to promote soil and water conservation, or to refinance debt.

Operating Loans

Guaranteed Operating Loans (OL) may be used to purchase livestock, farm equipment, feed, seed, fuel, farm chemicals, insurance, and other operating expenses. Operating Loans can also be used to pay for minor improvements to buildings, costs associated with land and water development, family living expenses, and to refinance debts under certain conditions.

Understanding Environmental Risk Analysis

Environmental Risk Analysis (ERA), also referred to as due diligence, is defined by FSA as the review of real property to determine the presence or likely presence of any hazardous substances, hazardous waste, petroleum products, or underground storage tanks (USTs). This review also seeks to determine the likelihood of past, present, or future releases of toxic or hazardous material into structures, the ground, the groundwater, or the land surface. The ERA includes inspecting the site and surrounding properties, surveying past ownership and uses of the property, and reviewing public records.

One of the main purposes of completing an ERA is to assess the environmental condition of a real property to determine what level of risk may be associated with a loan related transaction. In some cases, the cost of cleanup may greatly exceed the recoverable value of the collateral.

FSA requires that an ERA be completed for each guaranteed loan request involving real estate security. The purpose of this requirement is to ensure that adequate security value is obtained for the proposed loan, as well as establish a baseline condition document that may be useful to both FSA and the lender if liquidation action is warranted.

Background

Two important laws, the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA) and the Resource Conservation and Recovery Act (RCRA), contain specific provisions regarding the liability associated with the cost of cleaning up hazardous waste contamination on real property.

Both CERCLA and RCRA were amended in 1997 to provide better protection for lenders who acquire title to real property as a result of foreclosure or other loan servicing actions. Even though the amendments provided improved guidelines for determining a lender's liability, there is still a need to perform proper analysis of the potential environmental risks that may be associated with a particular real property.



Both CERCLA and RCRA allow exemptions from liability for lenders who do not participate in the management of a facility or operation. A lending institution should evaluate its actions to determine if they constitute “participating in the management” of an operation located on the real property collateral within the meaning of CERCLA. If the actions are considered to be participating in the management, the lending institution may lose its exemption from liability under CERCLA and RCRA.¹

Process of Completing an Environmental Risk Analysis

FSA requires that lenders requesting a loan guarantee complete an ERA for all real property that the lending institution will hold as basic security for the loan. This process can be completed by employees of the lending institution or by third-party environmental consultants.

An ERA can be completed using one of the following forms of documentation:

- Form FSA-851, Environmental Risk Survey
- ASTM E 1528-93 Standard Practice for Environmental Site Assessments: Transaction Screen Process (TSP)²
- Lender's environmental risk analysis form³

It is required that an employee of the lending institution or a consultant visit the real property to evaluate whether there is obvious visual evidence of environmental concerns. The loan applicant should also be interviewed to request relevant environmental information such as the present and past uses of the property and the occurrence of any contacts by Federal, state, or local government agencies concerning environmental matters.⁴

¹ FDIC Financial Institution Letter (FIL—14—93), dated February 25, 1993

² A lender may also opt to use a higher level of review such as the ASTM E 1527-94 Standard Practice for Environmental Site Assessments: Phase Environmental Site Assessment Process (Phase I ESA)

³ If a lender proposes to use an internal form, the form will need to adhere to the minimum requirements of the FSA-851 process and be approved by the FSA State Environmental Coordinator.

⁴ FDIC Financial Institution Letter (FIL—14—93), dated February 25, 1993



FSA recommends that all obvious uses of a property should be identified from the present, back to the property's first developed use or back to 1940, whichever is earlier. Some exceptions apply, in which case, most of the questions contained in an environmental risk analysis document can be answered in the negative and determine that no further inquiry is required. The preparer of an environmental risk analysis must exercise careful judgment to determine if all environmental conditions of the property have been adequately addressed.

The decision to research the use of a property back to 1940 is based in part on the fact that the 1940's marked a significant turning point in the production of certain chemicals. Since the 1940's, toxaphene and related organochlorine compounds have been manufactured for use as pesticides. Organochlorine compounds are of particular interest in researching the historical uses of a real property as these chemicals persist in the environment long after their initial use.

In determining when it is necessary to conduct research of a real property's ownership and uses back to 1940, the preparer of the ERA document should consider several issues:

- First, the type of property should be considered. For example, if the property is currently in agricultural use and a long history of agricultural use can be confirmed through interviews with the owner and neighbors, then this could suffice as documentation of past uses of the property. Quite simply, the preparer of the ERA would make a determination on a case-by-case basis that further investigation would only reveal the same conclusion. In documenting agricultural uses of a property, the preparer of the environmental risk analysis should always pay special attention to whether any owners ever operated an aerial crop spraying operation on the property.
- Second, other sources of useful information would be the land records and aerial photographs. The current property owner could be asked to produce a copy of his or her deed to show how long they have owned the property and from whom it was purchased. A review of the most recent aerial photography as well as older aerial photographs can reveal whether any industrial businesses or gas stations occupied the property.
- Federal and state agencies maintain lists of impacted or contaminated property. Many of these are available over the Internet. Two common sites are: www.epa.gov and www.rtk.net. Other state agencies may have websites of their own and some can be downloaded using various geographical information systems (GIS) programs.

Issues such as the following should be carefully observed and noted during the field visit. Photographs and maps should be included as part of the ERA document to illustrate potential areas of concern. In some cases, it may be necessary to obtain the opinion of trained professionals to evaluate the risk that may be present:

- **Underground storage tanks (USTs)**
 - Determine size, age, past testing, permits, contents, current use.
 - Check for visible leakage (dead or profuse vegetation, contaminated surface water, soil discoloration, odors, etc.).
 - Check whether state law requires all USTs to be removed.
- **Chemical storage/application**
 - Determine location, type of products, container storage and disposal methods, equipment cleaning areas, etc.
 - Check for visible leakage (dead or profuse vegetation, contaminated surface water, odors, etc.).
- **Livestock waste**
 - Are there surface waters nearby which have been or could be contaminated?
 - Is waste accumulating faster than disposal?
 - What is the disposal method and is it common to the area?
- **Area/neighborhood influences**
 - Are there environmental concerns in the local area that may influence the property?
 - Are there hazards on adjoining properties? (They may be just as detrimental as if the problem were on the property under consideration.)
- **Water quality**
 - A potable water supply for humans and livestock is critical whether the source is ground water or surface. This is relatively easy and inexpensive to check through state and local labs. Has the well water been tested? Some states require well water be tested at the time a property is sold. Water quality for crops should also be observed.
- **Developing issues**
 - Lead based paint in dwellings to be remodeled or razed Asbestos in the insulation of ducts, pipes, tile, and siding.

Addressing Potential Areas of Concern

If a lender discovers that a property has potential environmental concerns associated with hazardous substances or USTs, there are several possible solutions to reduce the potential liability that could be associated with involving itself with the property through a lien or mortgage:

- Require the loan applicant to conduct a clean up or remediation of the environmental risk in accordance with state and/or local environmental regulations. The applicant should be required to obtain any necessary clearance documents from the appropriate regulatory authority.
- Require the loan applicant to provide alternate security for the loan request. This would be security that is not affected by environmental risks.

If there is some question as to the severity of the environmental risk, the lender and applicant may choose to complete additional testing including collecting soil and water samples to verify the extent and severity of any potential contamination. The cost of this testing is negotiated between the lender and their applicant. There may be some assistance from various state programs.

For Further Information

Lenders participating in the guaranteed loan program should contact their local FSA office for further information regarding environmental risk assessment requirements associated with approval of a loan guarantee. Information may also be obtained by contacting the FSA State Environmental Coordinator located in the FSA State Office. Information may also be obtained about FSA's environmental and cultural resource compliance requirements at <http://www.fsa.usda.gov/dafp/cepd/epb/default.htm>.

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