

TO: State Directors, Rural Development

ATTN: Business Programs Directors, Rural Development Managers, Community Development Managers, and State Environmental Coordinators

SUBJECT: Business and Industry Guaranteed Loan and Section 9007 Rural Energy for America Programs
Transaction Screen Questionnaire and Phase I Environmental Site Assessments

PURPOSE/INTENDED OUTCOME:

The purpose of this Administrative Notice (AN) is to provide guidance on how to evaluate the economic impacts posed by contamination by hazardous substances or petroleum products when determining the liquidation value of real property in the Business and Industry (B&I) loan programs. This AN applies to RD Instructions 4279-A, 4280-B, and 4287-B.

COMPARISON WITH PREVIOUS AN:

This AN replaces RD AN No. 4309, dated September 17, 2007, which expired on September 30, 2008.

IMPLEMENTATION RESPONSIBILITIES:

In liquidation cases, it is the responsibility of the lender to obtain the maximum amount from liquidation. In the liquidation plan submitted to Rural Development, Business and Cooperative Programs, the lender provides an estimate of the fair market and the potential liquidation value of the collateral, if the current loan balance, including accrued interest, is less than or equal to \$200,000. An appraisal report by a qualified independent appraiser is required on all collateral securing loans where the current loan balance is more than \$200,000, including accrued interest.

EXPIRATION DATE:
November 30, 2009

FILE INSTRUCTIONS:
Preceding RD Instructions 4279-A, 4280-B, and 4287-B

The purpose of an appraisal report is to permit the lender along with Rural Development, Business and Cooperative Programs to determine the appropriate liquidation actions. Paragraph VI. A.4., of the “Lender’s Agreement,” Form RD 4279-4, requires that Rural Development, Business and Cooperative Programs share the cost of the appraisal report equally with the lender.

In order to formulate a liquidation plan which maximizes recovery, the collateral must be evaluated for the presence of contamination or the release of hazardous substances or petroleum products which may adversely impact the market value of the collateral. An appraisal which does not consider this aspect is incomplete and possibly misleading. Because these environmental evaluations are performed in conjunction with the appraisal process, the cost of these evaluations will also be shared equally between Rural Development, Business and Cooperative Programs and the lender.

An evaluation of the recognized environmental conditions of collateral is made by conducting environmental due diligence in conjunction with the appraisal. The term, “Environmental due diligence,” in the context of a real estate transaction, is the term used to describe the process of evaluating real estate for the presence of contamination from the release of hazardous substances, hazardous wastes, and petroleum products, and determining the impact, if any, the contamination has on the regulatory status or security value of the property. If contamination is present, the cost of environmental restoration activities can be estimated and used to adjust the market value of the collateral. The process of environmental due diligence is designed to reduce any uncertainties arising from any recognized environmental conditions of collateral and to meet the “appropriate inquiry” and “due care” provisions in the Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA), 42 U.S.C. 9601, *et seq.*

Rural Development, Business and Cooperative Programs considers the use of the (1) initial investigation using the Transaction Screen Questionnaire (TSQ), and (2) environmental professional evaluation using the Phase I Environmental Site Assessment (ESA) to conduct environmental due diligence. The TSQ and Phase I ESA standards are published by the American Society of Testing and Materials (ASTM E-1528 and E-1527 respectively) and are an adequate format for performing due diligence. It is not necessary to complete both steps in performing due diligence if (1) the TSQ concludes a Phase I ESA is unnecessary, or (2) a Phase I ESA is completed without using a TSQ. It is necessary only to complete the level of review required to ascertain and document economic risks posed by contamination.

ASTM Standard E-1528-06 states that the purpose of the Transaction Screen Process is to “define good commercial and customary practice in the United States of America for conducting a transaction screen for a parcel of commercial real estate where the user wishes to conduct limited environmental due diligence (that is, less than a Phase I Environmental Site Assessment).” However, performing the screening using the TSQ consistent with ASTM Standard Practice E-1528-06 does not satisfy the Environmental Protection Agency’s (EPA), “Standards and Practices for All Appropriate Inquiries” rule (40 C.F.R. Part 312), and will not

qualify Rural Development, Business and Cooperative Programs for the CERCLA landowner liability protections. However, the TSQ can be an effective screening tool, even if considered “limited” environmental due diligence, because it will screen out properties that pose very little risk of environmental liability from the need to conduct a Phase I. Therefore, it is important to properly conduct the TSQ screening in order to identify properties that should be subject to a Phase I ESA under ASTM Standard Practice E-1527-05.

The ASTM two-step due diligence process is further explained as follows:

The TSQ is the initial level of inquiry which evaluates recognized environmental conditions of collateral and concludes whether or not additional evaluation is necessary. The TSQ is a series of questions that determines the present or past land uses or activities which have or had the potential for adversely impacting the environmental conditions and market value of collateral. If the results of the TSQ are inconclusive, a Phase I ESA is needed. (If contamination or hazardous materials are obvious during site visit, the TSQ may be eliminated and a Phase I ESA conducted immediately.)

The next level of review, a Phase I ESA, may be necessary to clarify the issues raised by the TSQ. A Phase I ESA is a detailed investigation and evaluation of a property’s environmental condition and involves a review of all pertinent records, a site reconnaissance of the property, interviews with current and past owners or operators of the property, and the preparation of a narrative report communicating the findings and conclusions about the environmental condition of the property. The Phase I ESA should indicate whether there is a need for further detailed investigation, in the form of a Phase II ESA, to determine the extent of contamination, remediation measures and associated costs. The Rural Development, Business and Cooperative Programs and the lender, if further investigation is warranted, may share the cost of these additional investigations.

The Phase I ESA must be performed by environmental professionals. Such professionals must be trained in the fields of environmental science and engineering and have the experience necessary to perform the ESA, in accordance with the ASTM standards. The environmental professional must develop conclusions regarding the environmental status of a site and, if necessary, develop remedial options and estimate associated costs. This information is then shared with the appraiser so that a more accurate determination of market value can be made. Remediation plans proposed in ESAs need to be cleared with State or local agencies having jurisdiction over site remediation activities.

Rural Development, Business and Cooperative Programs consider ASTM standards to be an effective way to determine and document the recognized environmental conditions of collateral and reduce the potential effect that an adverse environmental condition would pose to the market value of the property, particularly at the time of liquidation. Lenders should contact the Program Director for further assistance in incorporating environmental due diligence into their liquidation

plans. The Program Director will contact the State Environmental Coordinator (SEC) for advice as needed. If environmental due diligence is to be conducted other than as stated in this AN, it must first be cleared with Rural Development, Business and Cooperative Programs in the National Office.

All Section 9007 Renewable Energy Systems and Energy Efficiency Improvement guaranteed loans are to be serviced in accordance with RD Instruction 4280-B, 7 C.F.R. section 4280.152.

If you have any questions, please contact the B&I Division, Servicing Branch at (202) 690-4103.

(Signed by Ben Anderson)

BEN ANDERSON
Administrator
Business and Cooperative Programs