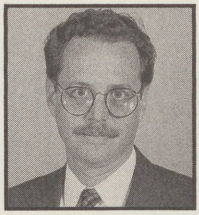
Environmental Considerations in Agriculture & Agribusiness Lending

by Steven C. Turner, John P. Heil and Anne M. O'Brien



Steven C. Turner is a Partner in the firm of Baird, Holm, McEachen, Pedersen, Hamann & Strasheim, in Omaha, Nebraska. He is a member of the American Bar Association and the Nebraska Bar Association. Mr. Turner is a member of the American Bar Association Committee on Commercial Financial Services and serves as the Chair of the Subcommittee on Agricultural and Agri-Business Financing. Mr. Turner's areas of practice include banking, loan transactions, bankruptcy and creditor's rights.

John P. Heil is a Partner in the firm of Baird, Holm, McEachen, Pedersen, Hamann & Strasheim, in Omaha, Nebraska. He is a member of the American Bar Association, the Nebraska Bar Association and the Florida Bar. Mr. Heil is a member of the American Bar Association Section of Natural Resources, Energy and Environmental Law and is a member of the National School Board Association Council of School Attorneys. Mr. Heil's areas of practice include environmental and litigation matters and school law.

Anne Marie O'Brien is an Associate in the firm of Baird, Holm, McEachen, Pedersen, Hamann & Strasheim, in Omaha, Nebraska. She is a member of the American Bar Association, the Nebraska Bar Association and the Missouri Bar Association. Ms. O'Brien's areas of practice include litigation and environmental matters.

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Introduction

Environmental concerns and risks may be present in many agricultural and agribusiness loan transactions. Businesses such as feedlot operations, grain elevators, co-ops, fertilizer and chemical dealers and suppliers, poultry operations, meat packing and rendering facilities, cattle ranches, hog production facilities, and traditional crop operations may generate, use, or dispose of hazardous materials or other wastes that pose a risk to the environment. The lender should assess these risks using a step-by-step analytical process in order to make informed decisions throughout the loan process.

Environmental Hazard Liability

An increasing sensitivity has developed in this country over the past two decades concerning the use and disposal of

hazardous substances. Congress as well as state legislatures have responded to this concern by enacting various regulatory and liability legislation to cleanup the environment and to deter activities contributing to the problem. Of major interest to lenders is the federal Comprehensive Environmental Response Compensation and Liability Act of 1980 (CERCLA), as amended by the Superfund Amendments and Reauthorization Act of 1986 (SARA).[1] The purpose of CERCLA and SARA is to establish liability and a procedural and financial mechanism to ensure cleanup of both active and abandoned properties contaminated with hazardous substances. CERCLA and SARA impose cleanup liability on the current owner of the polluted site, past site owners from the time of any disposal, parties that arranged for disposal, parties that accepted the hazardous waste for transportation to the site, and parties that operated the site.[2] A present owner is strictly liable even though the polluted land was acquired years after the hazardous waste was deposited.[3] Individual liability extends to a corporation's officers and employees actively involved in any of the corporation's handling of hazardous wastes.[4] A parent corporation that oversees and controls pertinent activities of a subsidiary corporation also may be held liable as the "operator" of a site.[5]

Cleanup liability under CERCLA and SARA includes natural resource damages as well as "response costs" incurred by the government and by other private parties at a polluted site.[6] Response costs are defined as expenditures for monitoring, assessing, and evaluating the site, interim protective measures, removal of the hazardous substances, and other remedial measures.[7] Such response costs have been known to exceed $1,000,000 just for the cleanup of a site less than one acre in size that was contaminated by spilled or leaking insecticides. The hazardous wastes to which CERCLA and SARA apply are determined by the Administrator of the U.S. Environmental Protection Agency and are listed in fine print covering more than 50 pages of federal regulations.[8] Included are chemicals and substances as common as asbestos, creosote, parathion, and malathion.

A lender is not liable as an "owner" under CERCLA and SARA simply because it has a lien or security interest in property contaminated by a hazardous substance.[9] Despite this, the lender can still be affected by the broad legislative reach of CERCLA and SARA. The value of any collateral securing a loan may be significantly impaired or destroyed by contamination with a hazardous substance. The borrower may default because it cannot afford the cost of cleanup or regulatory compliance. The lender may incur cleanup liability either by exercising sufficient control over the borrower or over the property to be determined an "operator" or by acquiring ownership of the contaminated property through foreclosure.

Because of the significant adverse potential, lenders must assess any possible environmental risks to the collateral or to the lender by completing an environmental assessment. This assessment can be accomplished in four stages: Pre-Loan Audit and Assessment, Loan Documentation, Post-Loan Monitoring, and Default and Lien Enforcement.

Pre-loan Audit and Assessment

In the past a lender considering a loan request would consider, among other items, the borrower's operation, management, cash flow; the market demand for

products; and the value of the collateral. In addition to determining the borrower's financial condition, the lender should complete a comprehensive environmental assessment and audit of the borrower's property and operation. This process consists of four steps: (1) a questionnaire, (2) a review of public records, (3) a visual and sub-surface inspection of the property, and (4) an assessment of any costs and changes in operations needed to make the property environmentally sound. Whether all four steps must be completed for a loan transaction will depend upon the results of each step. The information obtained during any particular step may demonstrate the need either to proceed with subsequent steps or to decline the loan.

Step One—Questionnaire

In step one the lender should obtain detailed information about environmental risks. This information can be acquired by submitting a questionnaire to the borrower or by reviewing the property and operation with the borrower. Make certain the questionnaire accurately identifies the businesses and properties that are to be part of the loan decision-making process. The following questions should be asked of the borrower:

1. Does your business use materials that may be hazardous? If so, give a detailed description of each or provide a copy of the Material Safety Data Sheet that accompanies hazardous products.

2. Does your business generate hazardous or other wastes as by-products? If so, give a detailed description of each waste by-product.

3. Have you or anyone else deposited, stored, used, manufactured, or generated hazardous materials or wastes on the property site? If so, give a detailed description of each.

4. Have you or anyone else ever used the property as a landfill, dump, or disposal site for any chemicals, compounds, or hazardous materials and wastes? If so, give a detailed description of the precise location, the dates used, the length of time used, the items disposed, and the methods of disposition.

5. To your knowledge, were asbestos products used in the construction or the improvements?[10] Is there any other asbestos on the property? If so, where?

6. List all substances that you, your agent, employees, or others disposed of as solid or liquid waste in your operation. For each such substance, indicate the manner of disposal.

7. If any of the substances listed above are to be or were disposed of on the property, give a detailed description of the disposal site and operations.

8. List all substances discharged into the atmosphere. State the date and the manner of the discharge.

9. List all substances stored on the premises, and describe for each the storage facility and its location. Include all underground storage tanks used or previously used on the premises. State the use, age, and capacity of each tank; note whether there is any indication of leakage from inventory records or otherwise, and state whether you or anyone has taken precautions to prevent deterioration or leakage.

10. List all substances discharged or previously discharged into surface or subsurface water on the property or into any sewerage or drainage systems. State the dates and the manner of discharge.

11. List each chemical or organic substance brought on to, stored, and or taken off of the premises. Describe how the substance is handled from the time it enters your property to the time it leaves your property. Include any chemicals applied to the land or its crops, describe each chemical, the brand name, manufacturer, the dates of application, and method of disposal or storage of any unused chemicals.[11]

12. Are any of the substances listed in your answers to questions 1 through 11 known to be hazardous to the environment? Do these substances contain material that is hazardous to the environment?

13. For each substance listed in your answers to questions 1 through 12 describe in detail the special precautions, if any, that you or others are taking to avoid contamination of the environment.

14. To the best of your knowledge, who has owned and operated the premises in the last 75 years?

15. What use has each previous owner made of the premises and what business was he or she engaged in?

16. Do you have or are you in the process of applying for any type of discharge permit for your operation? If so, list each permit and provide copies of all documents related to the application for that permit.

17. Has any governmental body (local, state, or federal) that has the responsibility for protecting the environment or public health contacted you or another person concerning the property site or your operation? If so, describe in detail the nature of the contact and provide copies of all documents related thereto.

18. State the dates of construction for each improvement on the property site.

19. Describe the type and operation of heating, cooling, and ventilating systems that are used on all improvements on the property site.

20. Has anyone performed tests, studies or analyses on any area of the property to determine the presence or absence of any hazardous substances, including asbestos, lead and radon? If so, provide copies of the test results and the names and addresses of all inspectors or auditors who conducted such tests.

21. List and provide the location of all wells on the property. For those wells that have been plugged or sealed, state the date and manner in which the wells were closed.

22. Who are the owners of adjacent and contiguous properties, and what type of businesses are they engaged in? Do any of these property owners process, use, store, apply, transport, manufacture, treat, or dispose of hazardous substances or waste? Are there any landfill or lagoon disposal facilities for liquid or solid waste nearby?

The information derived from these questions may indicate potential environmental hazards or risks: *(1) that are present on the site, (2) that are currently posed by the borrower's operation, or (3) that may arise in the future.* Responses

may indicate the presence of an environmental risk so great that the lender may decide not to extend the loan. However, the lender should not rely solely on this checklist, even if the responses do not indicate an environmental risk. The borrower may be unaware of all the potential environmental hazards on its property, or may think that past actions did not pose any risk to the environment. Therefore, if making a loan, he should complete step two, regardless of the responses provided in step one. Step two includes a search of the public records to determine if the borrower or any past or adjacent owners have been involved in environmentally hazardous activities.

Step Two—
Review of Public Records

The lender, an environmental engineer or consultant should check all local, state, and federal records to ascertain whether the borrower's operation, property, or any nearby properties or businesses present an environmental risk.[12] The U.S. Environmental Protection Agency (EPA) has a National Priorities List, which includes contaminated sites that the EPA has deemed in need of immediate rectification. The EPA's Regional Office for the borrower's state may also have information on local hazards that are not on the National Priorities List. Additionally, state environmental control agencies may have files on known or suspected pollution problems, information on the extent of any hazard, and records of any administrative or judicial enforcement actions.

Local property records, tax authorities, building inspectors, health officials, state environmental agencies, fire marshals, and local fire and water departments may also have information concerning:

1. Prior ownership and uses of the property

2. The status of any discharge permits

3. Location of any underground storage tanks on or near the property and whether any tanks have leaked; and

4. Any wells on or near the property, whether the wells are operating, and if they have been recently tested for contamination.

The lender should contact previous owners to determine how the property was used and whether or not there was any use, storage, application, treatment, or disposal of hazardous substances on or nearby the property.

Again, this review of public records may expose such significant environmental risk that the lender may decide not to extend the loan. However, if the review does not demonstrate significant environmental risk, then the lender should complete step three, a physical inspection of the property.

Step Three—
Site Inspection and Investigation

Step three involves two phases: (1) a visual inspection of the property site; and (2) professional testing and analysis to determine the extent of any potential risk.

Phase One. In phase one the lender and the environmental consultant should physically inspect the borrower's real estate and operation for signs of potential hazards. They should examine not only the property but also (a) any above or below-ground tanks, pits, ponds, pools, lagoons, or other storage and disposal sites for fuels, oil, chemical pesticides and fertiliz-

ers, or other chemicals; (b) the proximity of the property to other sources of hazardous exposure; and (c) any waste disposal systems for farm animals or industrial operations.[13] The following are among the signs of potential environmental hazards that may be visible during a physical inspection:

1. Darkened or stained soil, waterways or rocks

2. Dead, dying, or deformed crops or plant life that should be healthy

3. Dead, dying, or deformed fish, fowl, or other wildlife around streams, lakes, lagoons or wetlands

4. Unusual odors in unexpected places

5. Stagnant pools of unusual looking water or other fluids

6. Hazardous or improper use or operation of contiguous property involving hazardous materials or waste disposal.

If there is any waste disposal system for livestock or industrial operations, a consultant or engineer should determine whether it is operated in compliance with permits and local, state, and federal requirements. A similar determination should be made for irrigation systems used to apply chemical fertilizers, herbicides or pesticides.

If neither the site inspection and investigation nor the information from steps one and two reveal any environmental risks or a need for further investigation, the lender can determine whether to consummate the loan transaction. However, if the process discloses an existing or potential hazard or suggests a need for further inquiry, the lender should proceed to phase two of step three.

Phase Two. In phase two of step three, the lender should retain a qualified environmental engineer or geotechnical service for an in-depth, subsurface exploration of the property. Depending on the situation, such exploration may include (1) resource sampling of the soil, ground, and well water; (2) an examination of any substances in pits, lagoons, and ponds; (3) resource sampling of air in buildings; (4) resource sampling of waste streams; or (5) inspection of all improvements for the presence of hazardous materials on the property. This in-depth analysis should help expose the breadth of any actual or potential contamination so that the lender can make an informed decision in the next step of the environmental assessment process— economic analysis and appraisal.

Step Four— Economic Analysis and Appraisal

In step four the lender analyzes the economic risk in extending the loan. This analysis requires a property value appraisal and an estimate of the costs of removing any existing or potential environmental hazard. The lender then compares these two figures to determine the environmental impairment to the value of the collateral. If the impairment is significant, the lender should consider not extending the loan. If the environmental risk requires no immediate action or can be eliminated inexpensively, the lender nonetheless should exercise caution if the real estate at risk is to be the primary collateral for the loan. Experience has demonstrated that environmental hazards tend to be understated on discovery because of the difficulty inherent in making generalizations from the

limited data afforded by inspections and resource sampling. In addition, public concern about environmental issues is continuing to prompt new laws and more stringent regulations that will probably be retroactive.

Loan Documentation

Even if the lender has determined that there is no environmental risk or at most an acceptable level of risk, the lender should include certain terms and provisions in its loan documents to protect itself from past, present, and future environmental liabilities.

Commitment Letters. Any commitment letter should contain a provision stating that the loan is conditioned on an environmental audit not revealing the presence, release, or threatened release of hazardous materials, wastes, substances, pollutants, contaminates, conditions such as underground storage tanks, or any operations that may create future environmental liability problems. The commitment letter should specify which party is to pay for the cost of the environmental audit and assessment—a cost which the lender should attempt to transfer to the borrower.

Exclude Risky Assets. Excluding from the collateral base any assets that might be the source of an environmental hazard may diminish the risk of potential liability to the lender. For example, the lender could exclude from the collateral base any acres containing an underground tank, waste disposal lagoons, or chemical storage and mixing facilities. If, however, these items are an integral part of the borrower's operation and the going concern value of the collateral, then they should not be excluded even if they present an environmental risk.

Representations and Warranties. Lenders should require the borrower to represent (1) that neither the borrower, nor any prior owner or occupant created conditions that may give rise to environmental liabilities and (2) that no enforcement actions are pending or are threatened. The borrower should also covenant to remedy any present or future contamination; agree to comply with all local, state, and federal environmental laws; and grant the lender access to test and monitor the property in the future. Further, the lender should obtain a representation that the borrower has fully disclosed all conditions relating to any known existing environmental concerns.[14]

Indemnification. The lender should also obtain an agreement from the borrower indemnifying the lender from: (1) damage or costs related to the cleanup of hazardous waste or materials, including prior hazards undiscovered in the environmental assessment and any hazards that may occur during the course of the loan; (2) all costs and expenses that the lender may incur by reason of any inaccurate environmental representation or warranty of the borrower; (3) all foreseeable and unforeseeable consequential damages resulting from the use, generation, storage, or disposal of hazardous materials by the borrower or any prior owner or operator of the property; and (4) all costs of repair, cleanup, or detoxification of the collateral, whether or not such action is required by a governmental agency.[15] As with most indemnification agreements, the strength of these clauses will ultimately depend on the solvency of the borrower.[16]

Attorney Opinion Letter. The lender should request an opinion from the borrower's attorney regarding any potential environmental hazards associated with the

property. This opinion should include (1) a statement that the attorney has searched the records of all public health agencies and local, state, and federal environmental agencies and that no investigations, inquiries, or enforcement proceedings involving the site or adjacent properties have been undertaken; (2) whether the borrower's operation requires any permits and whether the operation adheres to local, state, and federal standards for waste disposal or water pollution control; and (3) whether the borrower is in compliance with permits and federal, state and local regulations.

Insurance. As a condition to the loan, the lender can require that the borrower obtain environmental insurance. There may be policies on the market that provide coverage for cleanup costs and damages. If obtained, the lender should insist it be named as an additional insured.

Cleanup costs are not normally covered by title insurance policies. However, some title insurance companies may add an environmental endorsement to their policies for residential properties. The endorsement will insure against only any loss or damage incurred if the lender loses priority of its lien on the property because a state or federal agency orders cleanup of a hazard. The latter endorsement would protect the lender in any "super-lien" state. (Super-liens are state priority liens arising from the cleanup costs of an environmental hazard. These liens grant the state first priority over all other liens and encumbrances, even those recorded before the super-lien was filed or before the hazardous release occurred.[17])

Notice, Default and Acceleration. The borrower should immediately provide the lender with any notice that the borrower receives concerning potential contamination, violations, or potential violations of environmental regulations or laws, or the commencement of environmental enforcement proceedings. The failure to provide such notice should constitute an event of default. In addition, the lender may require inclusion of provisions for acceleration of the loan in the event of any environmental enforcement proceedings or the discovery of any environmental contamination on the property.

The lender should not assume that incorporation of the above provisions into the loan documents will eliminate all environmental risk. These loan provisions are intended to help the lender avoid or lessen the risk of liability for cleanup costs and to provide the lender with some flexibility in dealing with environmental hazards. As a practical matter, once an environmental hazard is discovered on the property, the actual value of the collateral will be immediately diminished by at least the estimated cost of cleanup.

Post Loan Monitoring

After the environmental audit is completed and the loan is closed, the lender should consider the need to monitor the property for development of any environmental risks. Although an environmental hazard may not have existed at the time of the loan closing, the borrower's continuing use of the property or adjacent landowners' use of their property may create such a hazard. Accordingly, it is prudent to periodically audit or monitor the collateral for any problems, particularly if the nature of the borrower's operation could create such a risk (e.g., a meat packing facility, poultry operation, fertilizer manufacturer or distributor, or even a farmer/producer whose operation may be chemically intensive).

The need to monitor the borrower must be balanced, however, and monitor-

ing should not rise to the level of control of the borrower's operation. While a lender that merely holds a lien or a security interest in polluted property is not an "owner" liable for a cleanup cost judgment under CERCLA, a lender who is found to control or operate property contaminated with a hazardous substance is subject to cleanup cost liability. For example, a lender who becomes involved in the day-to-day management of a borrower to the extent that it controls the borrower's decisions involving operations or personnel, may be found liable as an operator for cleanup costs resulting from the borrower's mishandling or improper disposal of hazardous materials. Factors used by the courts to determine whether the lender is in control include the nature and extent of reports received from the borrower, the frequency of meetings between the lender's representative and the borrower, and the borrower's responsiveness to the lender's demands or requests. Operator liability for the lender may exist as long as it appears the lender was in charge, even if there is no direct connection between the acts resulting in the pollution and the lender's demands.[18]

Thus, the lender must be very cautious about becoming involved in the management and operation of the borrower's business. The lender can generally oversee the borrower's financial matters, but it must avoid any day-to-day, proactive entanglement in the management of the borrower's operation.

Default and Lien Enforcement

If the borrower defaults, the lender will need to consider its option to foreclose. Before doing so, the lender should again determine of all the risks and liabilities it will acquire in addition to the title to the property.

Under CERCLA and SARA, a lender who acquires contaminated property through foreclosure becomes its "owner" and may be liable for cleanup costs. Even an owner who acquires the property years after the substance was deposited can still be held liable because mere existence of hazardous waste on the property is enough to trigger cleanup liability. One lender that foreclosed its lein and took title to contaminated property was informed by a federal court that it was not exempt from liability under CERCLA and SARA. The court also warned the lender that CERCLA was not an insurance scheme for financial institutions and that mortgagees should protect themselves in the future by making prudent loans or by exercising the option of refusing to foreclose or bid at the foreclosure sale.[19]

This warning must be heeded. Prior to any foreclosure, the lender should conduct another environmental audit and assessment to determine whether it may become the owner of an environmental hazard. At this late point, the lender cannot rely on its pre-loan assessment because subsequent events on or near the property may have resulted in contamination. The pre-foreclosure audit should be at least as thorough, if not more thorough, than the pre-loan inquiry. Only a fully informed lender can make a prudent decision on whether to foreclose.

CERCLA and SARA establish an innocent landowner defense which exempts from liability any owner who had no knowledge or reason to know of hazardous waste problems on the property.[20] Thus, for a lender to establish that it acquired contaminated property without knowledge, it must demonstrate that it undertook an appropriate pre-acquisition inquiry into the previous ownership and uses of the property, all consistent with

good commercial or customary practices in an effort to minimize liability.[21] Factors used to determine whether the innocent landowner defense applies include (1) any specialized knowledge or expertise on the part of the purchaser; (2) the relationship of the purchase price to the fair market value of the property; (3) the value of the property if uncontaminated; (4) commonly known or reasonably ascertainable information about the property; (5) the obviousness of the presence or likely presence of contamination of the property; and (6) the ability to detect such contamination by appropriate inspection.[22]

Unfortunately, the innocent landowner defense may be useless as a practical matter for a lender who acquires contaminated property through foreclosure. Under the strict standards of inquiry it is difficult for any commercial party to establish that it made the necessary investigation, yet still did not discover or have reason to believe that the property contained significant hazardous wastes. In fact, the legislative history of CERCLA and SARA places a higher standard on those engaged in commercial transactions than on those engaged in noncommercial transactions.[23] Moreover, courts may impute that borrower's knowledge about the property to a lender if the lender had a history of financial dealing with the borrower or extensive involvement in the borrower's business.

To date there is little judicial guidance as to what constitutes a "due diligence" inquiry. An EPA Guidance on Landowner Liability issued in June 1989 didn't address questions on how to avoid such liability. Further, counsel for the EPA suggested that there will be no forthcoming guidance on this issue. Therefore, a prudent lender should conduct an audit and assessment of the collateral using the four step process outlined above to decide if indeed it is in its best interest to foreclose on any collateral.

Another way in which a lender may be liable for cleanup costs is through actions taken to recover collateral. For example, if a lender retains a liquidator to enter the borrower premises and remove equipment and hazardous substances are released or spilled during this process, then the lender can be found jointly and severely liable with the borrower for the entire cleanup costs associated with the property. In this instance, the lender's liability may be based on having "arranged for disposal" of a hazardous substance at the contaminated site (albeit inadvertently), or the lender's liability may be based on having "operated the site" (albeit only temporarily and only through the acts of its contractor).[24]

Conclusion

A lender must be aware of environmental considerations throughout each stage of the loan process because of the serious potential for impairment of the collateral and the imposition of lender liability. While exhaustive subsurface sampling and professional inspections of all improvements for each loan transaction could provide the lender with a high degree of assurance the cost would be prohibitive for most routine agricultural loan transactions. For this reason the step-by-step approach outlined above is the most economical and practical approach to minimizing the lender's risk of loss due to environmental hazards.

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[1]42 U.S.C.A. 9601 et seq. (West Supp. 1989).

[2]42 U.S.C.A. 9607(a) (West Supp. 1989).

[3]e.g., *New York v. Shore Realty Corp.*, 759 F.2d 1032 (2d. Cir. 1985).

[4]e.g., *U.S. v. Northeastern Pharmaceutical Chemical*

Co., 810 F.2d 726 (8th Cir. 1986).

[5]e.g., *Idaho v. Bunker Hill Co.*, 635 F.Supp. 665 (D. Idaho 1986).

[6]42 U.S.C.A. 9607(a)(4) (West Supp. 1989).

[7]42 U.S.C.A. 9601(23)-(25) (West Supp. 1989).

[8]40 C.F.R. 302.4 (1988).

[9]42U.S.C.A. 9601(20)(A) (West Supp. 1989) exempts from the definition of "owner or operator" any "person, who, without participating in the management of . . .[the property], holds indicia of ownership primarily to protect his security interest in . . .[the property]."

[10]Several courts have declared that CERCLA was not intended to allow for recovery of costs incurred in the removal of asbestos in buildings. *Retirement Community Developers, Inc. v. Merine*, No. AN-87-2464, slip op. (D.Md. 1989); *3550 Stevens Creek Assoc. v. Barclays Bank of California*, No. C-87-20672 RPA, slip op. (D.C. N. Cal. 1988). Legislation has been proposed to eliminate this gap in CERCLA. See, 20 U.S.C. 3601-3611, 4011-4022.

Further, lenders should be aware that in 1987 Congress considered extending asbestos abatement standards now in existence for school buildings to commercial and public buildings. (See Sen. 981, known as the "Toxic Substances Control Act of 1987"). Congress has postponed any further action on this bill until 1991, and it is uncertain whether it will ever be passed. A prudent lender, however should be aware of this possible legislation and should consider its impact on lending practices.

[11]Pesticides are within CERCLA's coverage. Title 42 U.S.C. 9607(i) provides that no person may recover "response costs or damages resulting from the application of a pesticide product registered under the Federal Insecticide, Fungicide, and Rodenticide Act (7 U.S.C. 136 et seq.)." This provision applies only to the application of pesticides and does not relieve any person of liability for the release of a hazardous substance. In fact, many cases relating to the cleanup of hazardous waste sites have involved the disposal of pesticides. 2 F. Grad, Treatise on Environmental Law 8.05, pg. 8-140 (1989).

[12]An environmental engineer or consultant with a proven and reputable track record should be able to conduct a comprehensive record search and identify all major hazards that are visible on the site. Most state environmental agencies can recommend consultants in private practice who have experience in this area. The lender should be cautioned, however, that traditional land appraisers are not generally trained to detect environmental problems, and the lender should not rely on an appraiser to assist it in discovering and investigating environmental risks.

[13]If, for example, the property is located next to a dumping ground for hazardous chemicals, the borrower could be liable if the dumping extended to the borrower's land. In addition, the borrower's property or its water supply could be rendered useless due to the spreading plume of pollution from nearby environmental hazards. Most states have enacted detailed regulations governing disposal of animal wastes.

[14]Suggested language:

Borrower certifies that it has exercised due diligence to ascertain whether the premises or any site within the vicinity of the premises is or has been affected by the presence of asbestos, radon, lead, hazardous or nuclear waste, toxic substances, or other pollutants or hazardous wastes or materials that could be a detriment to the premises or its value. Borrower further certifies that it has exercised due diligence to ascertain whether the premises or any operation thereon violates any local, state or federal laws, regulations or standards.

If the lender wants to transfer to the borrower the responsibility of reviewing the public records of various enforcement agencies, it can also adopt the following clause into its loan documentation:

Borrower has made a written investigation to the appropriate National and Regional Office of the Environmental Protection Agency, the appropriate State Department of Environmental Protection and other similar local governmental agencies. None of these agencies have indicated that the collateral, any site in the vicinity of the collateral, or borrower's operation is or has been the subject of any hazardous material activity. Original correspondence from each agency stating the same is attached hereto.

[15]Suggested Indemnification and Hold Harmless Agreement:

1. Borrower, its successors and assigns, and Borrower's guarantors (collectively referred to in this Paragraph 1 as "Borrower") agree to defend, indemnify, and hold harmless Lender, its directors, officers, employees, agents, contractors, sub-contractors, licensees, invitees, successors and assigns (collectively referred to in this Paragraph 1 as "Lender"), from and against any and all claims, demands, judgments, damages, actions, causes of action, injuries, administrative orders, consent agreement and orders, liabilities, penalties, costs, and expenses of any kind whatsoever, including claims arising out of loss of life, injury to persons, property, or business or damage to natural resources in connection with the activities of Borrower, its predecessors in interest, third parties who have trespassed on the Premises, or parties in a contractual relationship with Borrower, or any of them, whether or not occasioned wholly or in part by any condition, accident, or event caused by any act or omission of Lender, that:

(A) Arises out of the actual, alleged or threatened discharge, dispersal, release, storage, treatment, generation, disposal or escape of pollutants or other

toxic or hazardous substances, including any solid, liquid, gaseous or thermal irritant or contaminant, including smoke, vapor, soot, fumes, acids, alkalis, chemicals and wastes (including materials to be recycled, reconditioned or reclaimed); or

(B) Actually or allegedly arises out of the use, specification, or inclusion of any product, material or process containing chemicals, the failure to detect the existence or proportion of chemicals in the soil, air, surface water or groundwater, or the performance or failure to perform the abatement of any pollution source or the replacement or removal of any soil, water, surface water, or groundwater containing chemicals.

2. The Borrower, its successors and assigns, shall bear, pay and discharge when and as the same become due and payable, any and all such judgments or claims for damages, penalties or otherwise against Lender described in Paragraph 1, and shall hold Lender harmless for those judgments or claims, and shall assume the burden and expense of defending all suits, administrative proceedings, and negotiations of any description with any and all persons, political subdivisions or government agencies arising out of any of the occurrences set forth in Paragraph 1.

[16]The provisions of any non-recourse loan should be modified to impose liability on the borrower for the breach of any environmental warranties, cleanup of any environmental hazard, and for any amounts paid by or adjudged against the lender for cleanup, cleanup costs, or environmental damages.

[17]Some states created super-liens in order to expedite the resolution of environmental problems caused by a release of hazardous material and to recover any cost of cleanup eventually borne by the state. The lender should determine before making a commitment to a borrower whether the collateral is located in a super-lien state. If so, the lender's security interest is junior to the state's interest if the state has paid for the cleanup of that collateral and that collateral contains an environmental hazard. Some super-lien states include Connecticut [Conn. Gen. Stat. Ann. 22a-452a (West. Supp. 1988)]; Idaho [Idaho Code 539-4431 (1985)]; Illinois [Ill. Ann. Stat. ch. 111 1/2 1021.3 (Smith-Herd)]; Main, [38 ME. Rev. Stat. Ann. 1371 (Supp. 1988)]; Massachusetts [Mass. Gen. Laws Ann. ch. 21E (West Supp. 1988)]; Michigan [Mich. Comp. Laws Ann. 299.543(3) (West Supp. 1988)]; New Hampshire [N.H. Rev. Stat. Ann. chap. 147B (Supp. 1988)]; and New Jersey [N.J. Rev. Stat. 58:10-23:11, et seq. (Supp. 1988)]. This list is not comprehensive.

[18]e.g., *U.S. v. Mirabile*, C.A. No. 84-2280, slip op. (E.D. Pa. Sept. 4, 1985).

[19]*U.S. v. Maryland Bank & Trust Co.*, 632 F.Supp. 573 (D. Md. 1986).

[20]See 42 U.S.C.A. 9601(35)(B) (West Supp. 1989).

[21]Ibid.

[22]Also note that under 42 U.S.C. 9601(35)(C), even if an owner otherwise qualified for the third party defense obtained actual knowledge of the hazardous substance during its ownership of the property and subsequently transferred the property to another person without disclosing such knowledge, the third party defense is unavailable.

[23]*Conference Report No. 962*, 99th Congress, 2d Session, at 187-88 (1986).

[24]See e.g., *U.S. v. Fleet Factors Corp.*, 724 F.Supp. 955, 960-61 (S.D. Ga. 1988); *U.S. v. NEPACCO*, 579 F.Supp. 823 (W.D. Mo. 1984), aff'd in part 810 F.2d 726 (8th Cir. 1986).