

ARTICLES

Cradle-to-Grave Lending Risks Lurk after Natural Disasters

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We've all witnessed the harrowing broadcasts of tornadoes and hurricanes ripping through cities, blowing apart buildings and forcing thousands of people into shelters. We've also seen the follow-up footage of storm victims getting back on their feet and businesses reopening. But the lurking long-term effects of catastrophic storms almost always fly under the radar. Lenders who aren't protected from those ongoing effects are as vulnerable as when a storm first makes landfall.



To understand the liability banks and lenders might incur when making loans to developers in storm-affected areas, we first need to understand how detection and enforced remediation of environmental problems takes place in the aftermath of a hurricane.

Flooding, not wind, has the most long-term environmental impact and leaves places like Houston struggling for many years after impact. Flooding can compromise underground storage tanks filled with gasoline and chemicals. When businesses like dry cleaners are flooded, chemicals and toxins are released into the soil. That contamination can spread to surrounding areas in unpredictable ways. You may not even know that your business or home is sitting on contaminated ground because much of it goes undetected for years.

Regulation and enforcement is a trickle-down process. At first, regulators go after the most obvious cases. For example, the [Arkema chemical plant that flooded and partially exploded](#) during Hurricane Harvey received a lot of media attention, and has been under scrutiny by the EPA ever since.

Most contamination, however, isn't detected until a home or business is sold, or a developer comes in with a new project. Transactions can uncover where contamination lies. During the due diligence phase and environmental assessments, it might be discovered that a site has been affected, and will require extensive remediation measures.

Rebuilding in places like Houston requires both developers and banks willing to take on measured risk. Developers can mitigate their risk through environmental insurance products. In fact, the return on investment for these developers can be well worth the risk because they're buying undesirable sites below premium price.

Banks, however, have a host of other issues they need to be aware of. Most notably, when a bank makes a loan to a developer for a contaminated site and there's a default on the loan, if the bank forecloses on the property and assumes ownership of the property they may ***become responsible for the cleanup.***

Federal statutes give the government authority to control hazardous waste from "cradle-to-grave."

In other words, if you own a hazardous waste site, you can be forced into a remediation project to clean it up for as long as the contamination exists.

We've worked on sites that sat dormant for ten to 20 years and we've worked with a lot of lenders on risk for these types of loans. To protect themselves, banks can put processes into place to mitigate their risk when they sign new loans, but that's not enough. They need to look at all the loans they have on their books that were made before those processes were put in place.

Another vulnerability banks face is taking on existing loans through mergers and acquisitions. When consolidation occurs, the acquiring bank needs to know what due diligence the acquired bank did on loans that might involve contaminated sites and costly remediation issues down the road. Lenders need to protect themselves from becoming the deep pocket in the event the lender is brought into a remediation through a foreclosure. This potentially could open them to liability through the Strict, Joint and Several Liability statutes.

People have a tendency to underestimate the environmental conditions that can be caused by events like Hurricane Harvey. Lenders are an important part of the rebuilding effort, but they need to protect themselves against cradle-to-grave liability and make sure their risk is mitigated. For help in understanding your environmental risks, contact our team at environmental@risk-strategies.com.

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