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Brownfield Challenges May Present Advantages

Brokers can find a new niche in contaminated properties

By **Edward K. Elanjian**, executive vice president and chief financial officer, EnviroFinance Group LLC

COMMERCIAL MORTGAGE BROKERS seeking a new niche might want to consider brownfields. According to the U.S. Environmental Protection Agency, these properties are defined as those that “may be complicated by the presence or potential presence of a hazardous substance, pollutant, or contaminant.”

Generally, this contamination results from the prior use of the property or a neighboring property. Typical examples include former mining or industrial sites, gas stations and dry cleaners.

There are advantages to brownfield development. First, fewer buyers typically seek these properties. Additionally, brownfields are frequently found in blighted urban areas. This often yields less resistance to development and valuable sources of soft capital such as grants, tax credits and other economic incentives.

Other advantages can include price discounts when compared to similar noncontaminated property. Moreover, it's common for brownfields to be located near transportation centers, existing utilities and community infrastructure.

When it comes to financing these properties, mortgage brokers must understand the special requirements that come with the territory. Anyone who has tried to get nonrecourse financing on a property with a less-than-clean Phase I or Phase II environmental site assessment knows that brownfield financing can be scarce.

In the past, some conventional lenders made occasional brownfield loans to accommodate long-standing customers, often requiring additional collateral. Such risk-based lending has

succumbed to the credit crisis and is rarely available anymore. With a proper understanding of the real estate and remediation, however, these projects can be financed through specialty lenders.

Added complexities

Brownfield loans typically have advances for acquisition, remediation costs, soft costs and more. They also typically have an interest reserve with the interest rate adjusted to reflect the property's exposure. Though they can be more expensive and time-consuming than conventional loans, they often are cheaper than equity funding.

A typical loan term is two years. Extensions often are available if the remediation process isn't complete.

Lenders look at various factors when deciding whether to finance brownfields. The real estate must make sense and be properly priced; the project budget should be well-defined with significant cash equity; and there must be a sound exit strategy.

Included in these projects' complexities are the necessary dealings with regulators, who are more focused on public health and safety than on community development or redevelopment. In addition, brownfields present additional, surmountable engineering challenges and legal liabilities. These provide opportunities for mortgage brokers and developers with the financial and technical capabilities to navigate these roadblocks.

Environmental insurance

Basic environmental-insurance products may or may not apply to brownfield loans. Their

necessity directly relates to the size and complexity of the environmental risks. Generically, these products include pollution-legal-liability insurance, which covers tort claims and known or unknown conditions, and cost-cap insurance, which covers remediation-cost overruns.

Although brownfield lenders don't expect mortgage brokers to understand the loan's environmental aspects, they do expect brokers to understand the credit. Brownfield-loan packages are prepared just like other loan requests. They also require the most-recent environmental report, which should have the history of the investigation and remediation to date.

Brokers are compensated based on a signed fee agreement. There is also an opportunity to score twice with brownfield loans. Brokers can do this by maintaining contact with their clients and helping them with the funding that typically follows and repays a brownfield loan. **■**



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