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Learners Guide

COURSE TITLE

Opportunity Zones: Commercial Real Estate Investing and Environmental Site Assessments

COURSE DESCRIPTION

In this introductory course to Opportunity Zones and Environmental Site Assessments, brokers and appraisers can learn more about opportunity zones investments. Throughout the course, explore the rules and regulations for Qualified Opportunity Funds (QOFs) and Opportunity Zones (QOZs). From your role as a broker or appraiser, you will hear from industry experts on what these investment opportunities are, how to invest, and when. Once you understand these concepts, you will be in a better position to assist your clients to make optimal real estate decisions. Additionally, this course covers the due diligence an investor ought to do before putting money into an opportunity zone. Specifically, a smart investor should have environmental site assessments performed. There are multiple types of environmental site assessments, so it is necessary for brokers and appraisers to understand what they are and when they should be performed. Through this course not only brush up on your knowledge of opportunity zones and environmental assessments but have the foreknowledge to effectively guide your clients.

INDUSTRY EXPERTS

- Stephanie Trueb, ESA Technical Director - Real Estate Services, EBI
- Joseph Derhake, CEO and Founder, Partner Engineering and Science, Inc.
- Holly Neber, CEO, AEI Consultants
- Elizabeth Krol, PG, National Client Manager, Partner Engineering and Science, Inc.
- Jenny Redlin, REPA, Principal, Partner Engineering and Science, Inc.
- Nicole TK Moore, REPA, Technical Director, Partner Engineering and Science, Inc.
- Kristine Macwilliams, PE, Partner Engineering and Science, Inc.

COURSE LEARNING OBJECTIVES

At the end of the course, learners will be able to:

- Define opportunity zones and environmental site assessments
- Define the history and financial benefits of opportunity zones
- Compare and contrast Phase I and Phase II environmental site assessments
- Distinguish optimal moments to invest in opportunity zones and performing environmental site assessments
- Articulate the purpose and use of Opportunity Zone Funds
- Explain quality Opportunity Zone Funds
- Recognize the rules and regulations which dictate Opportunity Zone investments
- Breakdown the relationship between opportunity zones and gentrification
- Analyze how to choose sites for optimal business objectives

- Determine how to manage environmental and physical building risk, project completion and budget
- Characterize beneficial qualities and credentials of Environmental Consultants
- Determine quality due diligence for CRE acquisitions
- Define a Phase 1 environmental site assessment
- Determine when to perform a Phase 1 environmental site assessment
- Explain Phase 1 environmental site assessment legalities and recommendations
- Determine when to perform a Phase II environmental site assessment
- Describe Phase II environmental site assessment challenges, and Brownfield sites
- Differentiate between the misconceptions and facts of opportunity zones

COURSE INTRODUCTION

Opportunity Zones have been a hot-button topic in the real estate investment world for the past several months. The action has heated up even more since October 2018, when the U.S. Treasury Department provided some clarity on the rules by which Opportunity Zone investments can be made – one of which extracted a big sigh of relief among potential investors and developers. “Other than interest rates, I can’t think of another topic I’ve been more frequently asked about,” said Darin Mellott, CBRE’s Director of Research-Americas.

These opportunities zones are great real estate investments, but they require the investor and all parties to be aware of specific rules and regulations related to opportunity zones. Part of that due diligence includes having environmental site assessments performed based on the type of property. There are multiple types of environmental site assessments, so it’s necessary for brokers and appraisers to understand what they are and when they should be performed. Through this course not only brush up on your knowledge of opportunity zones and environmental assessments but have the foreknowledge to effectively guide your clients.

MODULES

Module 1: WHAT ARE OPPORTUNITY ZONES?

Introduction

The concept of Opportunity Zones was hatched in early 2017 by Sens. Tim Scott (R-SC) and Cory Booker (D-NJ) as a way to propel economic development in what the Internal Revenue Service calls “distressed areas.” Congress approved the legislation as part of the tax-reform bill last December. That was appropriate, since the investments in Opportunity Zones are “really tax-driven,” said Matt Ertman, a partner with the Allen Matkins law firm, which is working with several clients on Opportunity Zone issues.

Opportunity Zone investments are primarily a way for investors to defer capital gains taxes for a period of time.

LESSON 1: DEFINITION

The investor takes the proceeds from the sale of a property or security and re-invests them in a Qualified Opportunity Fund (QOF), which anyone can establish – investor, developer, etc. – though investors have started a smaller share of the funds than other groups The fund then finances the development or redevelopment of a property or properties within one or more Qualified Opportunity Zones (QOZ). The fund can be of any size, as long as the proper paperwork is fled by the tax deadline, according to a CNBC article.

In short:

- QOF investors can defer paying taxes on the capital gains used to fund their QOF investments until Dec. 31, 2026 – meaning they have to pay the taxes in April 2027, or when they sell the investment, whichever comes first.
- Those investors who hold their investments for five years get a 10% break on those original capital gains.
- QOF investors who hold their investments for seven years get a 15% break on those original capital gains.

In other words, the real-estate investor does not invest directly in the property, but instead invests in the QOF, which determines the properties it will fund. Of course, the fund's prospectus will tell potential investors where and what the investments will build or rebuild. This mechanism differs from, for example, 1031 exchanges, in which an investor can roll over gains from the sale of one property into investment into another – although both are geared toward capital-gains-tax deferral.

LESSON 2: HISTORY

In 1948, the United States launched the Marshall Plan, with the goal of providing $13 billion of capital and assistance for rebuilding Europe following the destruction of World War II. Close to 70 years later, the Tax Cuts and Jobs Act introduced another rebuilding effort, the Opportunity Zone program.

On the surface, there is a huge inherent difference between rebuilding post-war Europe, and working to economically sustain lower-income areas. However, in his column, "Opportunity Zones and Human Capital: Insights from the Marshall Plan," G. Lamont Blackstone with Project REAP attempted to link these two financial projects. Specifically, he spelled out that the importance of OZ success initiatives would depend on "the importance of cultivating local human capital for a redevelopment effort."

The Marshall Plan provides a good example of such capital, he noted, as it leaned heavily on local human capital for Europe's rebuilding efforts. Throughout that effort, corporate managers from European countries "were invited to learn modern management skills through study trips to the United States," Blackstone said. As such, capital being funneled into Qualified Opportunity Funds also provide ample opportunity for cultivating human capital for redeveloping inner-city and lower-income neighborhoods.

The benefits of such cultivation are that:
1) Including women and minorities at all levels of the investment process will "maintain a favorable legislative environment for the incentives," Blackstone pointed out.
2) Bringing talented minorities into commercial real estate deals can help boost understanding of local markets and business practices.

Blackstone continued his commentary by noting that “the pools of minority talent to support the impending capital flows into Opportunity Zones already exist” — or, if they don’t exist, they are out there to be hired. Project REAP (the Real Estate Associate Program) is, in fact, continuing to educate and promote minority talent to work with developing Opportunity Zones.

As funding for Opportunity Zones continues moving forward and being refined, “CRE executives should be cognizant of the role that human capital plays in redevelopment projects,” Blackstone concluded.

The Opportunity Zone program tucked within the Tax Cuts and Jobs Acts of 2017 focuses on pouring billions of capital gains into lower-income and economically disadvantaged areas. There have been some questions, however, as to whether some of those government-designated zones are already undergoing the process of gentrification. The concept of Opportunity Zones was hatched in early 2017 by Sens. Tim Scott (R-SC) and Cory Booker (D-NJ) as a way to propel economic development in what the Internal Revenue Service calls “distressed areas.” Congress approved the legislation as part of the tax-reform bill last December. That was appropriate, since the investments in Opportunity Zones are “really tax-driven,” said Matt Ertman, a partner with the Allen Matkins law firm, which is working with several clients on Opportunity Zone issues.

LESSON 3: FINANCIAL BENEFITS

- Even though Opportunity Zones’ designations are slated to expire at the end of 2028, investors can keep the investment with full tax breaks through 2047.
- On April 17, 2019 the U.S. Department of the Treasury issued its second round of guidance for the Opportunity Zones program. The latest information helped clarify some issues connected with the program.
- One important clarified issue focused on a Qualified Opportunity Fund’s asset sale while another clarification involved tax benefits for refinancing proceeds and secondary market purchase.

Another difference between QOZ investments and direct real estate investments is, as Allen Matkins partner Mike Pruter said, “two timing elements.”

“First, the investor must invest the capital gain (into a QOF) within 180 days of when the gain occurred,” said Pruter, who specializes in the tax aspects of real estate law. “This is unlike usual real estate funds, which lines up investors, calls capital and takes the time it needs to make the investment. Here, you have to structure the resources and get all the cash up front.”

Then, the investment itself needs to meet certain requirements. The funds are tested twice a year, Pruter said, and if the capital is not adequately deployed – primarily meaning that 90% of its assets are invested in a QOZ property – the fund is assessed a penalty of 5% per year. At some point, a non-complying fund could even be de-certified, “but the IRS hasn’t come up with a process to do that,” Pruter said.

The QOF also has 30 months from the time of initial investment to double the value of the development being funded. That means just the buildings, Treasury’s October guidance stated.

That's what caused the sighs of relief among investors and developers, because many feared the value of the land would be included in the improvement requirements. But it's not, which is piquing interest among more potential investors.

Even though the deferral on the original capital gains ends – for now – in 2026, those who keep their QOF investments for 10 years or more will not be assessed capital gains taxes on the improved value of the property invested in. For example, if a building was worth $50,000 when bought by the fund, and is worth $125,000 in 10 years' time, the investor won't have to pay capital gains tax on that additional $75,000.

And, even though Opportunity Zones' designations are slated to expire at the end of 2028, investors can keep the investment with full tax breaks through 2047.

As with any investment, potential investors must research QOF's background and the viability of the projects planned.

On Wednesday, April 17, 2019 the U.S. Department of the Treasury issued its second round of guidance for the Opportunity Zones program. The latest information helped clarify some issues connected with this tax-incentive program, which had been passed as part of the Tax Cuts and Jobs Act of 2017. The guidance cleaned up questionable topics, ranging from leases, to Qualified Opportunity Zone Businesses (QOZB), to better treatment of land which was, according to Greenberg Glusker's Schuyler Moore: "a huge issue."

The experts agreed that one important clarified issue focused on a Qualified Opportunity Fund's asset sale. "Now, if the QOF sells an asset, a partner can elect to exclude any gain flowing from a partnership or S-Corp to their K-1, so long as interest in the fund has been held for at least 10 years," said Marc Wieder with Anchin Accountants & Advisors. Prior to the guidance clarification, he noted, partners had to actually sell their QOF interest for that exclusion. "Now, if a fund with multiple assets sells one, it won't automatically trigger a gain for fund holders," he said.

Another important issue involved tax benefits for refinancing proceeds and secondary market purchase. Cadre's Dan Rosenbloom said that, distribution of refinancing proceeds doesn't trigger deferred gain recognition, nor does it preclude investors from eliminating capital gains tax, predicated on a 10-year hold. "Given the frequency of refinancing in real estate deals, and the potential need to use those proceeds to satisfy the deferred tax liability," Rosenbloom said, "this was welcome guidance."

LESSON 4: WHERE ARE OPPORTUNITY ZONES?

Qualified Opportunity Zones – recommended by the governors of each state and certified by the federal government – **are mostly in urban areas, though about one-quarter are in rural locations**. They are available in all 50 states, the District of Columbia, Puerto Rico and other U.S. territories.

Though the tax deferral portion of the Opportunity Zone program is attractive to many investors, KPMGs H. Robert Boehringer III sounded a note of caution. Namely, "there must be a business case and sound due diligence to support the ultimate project decision," he wrote in a recent article for Area Development Magazine. "The fact that an investment is located within an Opportunity Zone will not alone guarantee success."

Not all Opportunity Zones are created equal. While location analysis and site selection for new investment projects is a complex task even under typical circumstances, locating an Opportunity Zone investment can be more challenging. Boehringer noted that successful investment in these zones will require a well-versed project team, along with multiple factor analyses and an ability to make timely decisions.

With 8,700 designated Opportunity Zones in the United States, Boehringer suggested several considerations to selecting the right investments, in the right locations, for the right project, as follows:

- The location should be compatible with the targeted investment outcome.
- The site should be capable of meeting Opportunity Zone site constraints.
- The investor should understand the state and local tax implementations of Opportunity Zone investments.
- The investor should understand if the desired social contribution can be achieved through the Opportunity Zone investment.
- An exit strategy should be in place.

Boehringer went on to say that developers also need to step up and do more than market available sites and a community's specific attributes. Those developing within the designated zones need to create what Boehringer called the "required Opportunity Zone investor mindset."
"Economic developers must also be prepared to explain their project sites in a way they haven't in the past," he added. And finally, time is of the essence on potential Opportunity Zone investments.

MODULE 1: QUIZ—5 Minutes

Module 2: WHAT ARE QUALITY OPPORTUNITY FUNDS?
Introduction

- Much of the coverage of Qualified Opportunity Funds has focused on tangible investments like development and/or renovations of commercial real estate. However, little has been discussed about the QOF sub-fund.
- A QOF might choose to invest in a sub-fund which, in turn, funnels money into Qualified Opportunity Zone (QOZ) property.
- There are several ways to protect yourself when investing in QOFs and sub-funds.
- Due diligence is required for any investment; this is especially the case for QOF and sub-fund investments.
- QOFs and sub-funds must pass an asset test every six months. Additionally, QOZ properties in which a QOF/sub-fund invests are required to be "substantially improved" within 30 months.

Lesson 1: Similarities to Sub Funds

Coverage of the Tax Cuts and Jobs Act's Opportunity Zone program and Qualified Opportunity Funds (QOF) has been thorough and intense. However, much of that coverage focuses on tangible investments — such as development and/or renovations of commercial real estate. Little has been discussed about another QOF investment vehicle: the sub-fund. QOFs and sub-funds are subject to specific guidelines. However, some requirements for QOFs and sub-funds differ.

A QOF might choose to invest in a sub-fund which, in turn, funnels money into Qualified Opportunity Zone (QOZ) property. QOFs and sub-funds have several things in common:

- Both must be formed as corporations or partnerships (such as LLCs with multiple owners). Most QOFs and their sub-funds will be formed as LLCs, with multiple owners, partnership participation and pass-through taxation.
- Both must be created in the United States, or within U.S. possessions. Regarding the latter, a QOF or sub-fund is formed in U.S. possessions only if it will invest within a designated QOZ there.
- For both QOFs and sub-funds, tax benefits only apply if the entities acquire QOZ assets after 2017.

Lesson 2: Tax Benefits and Guidelines

If it sells interest from a sub-fund or property, the QOF is allowed a "reasonable period" to reinvest the gain. However, owners will pay taxes on that gain, unless it is re-invested in the same or different fund or used in a 1031 exchange.

Though the QOF and sub-fund have similar requirements, confusion occurs because of different guidelines, listed below:

- A QOF must hold 90% of its gross assets in QOZ property or sub-fund interests. The sub-fund in which that QOF invests only requires 70% its tangible assets be held in QOZ property.
- If the QOF doesn't meet the asset test of 90%, it pays a 5% interest penalty on the shortfall. If the sub-fund fails to meet the 70% asset test, it immediately is disqualified.
- An entity declares itself a QOF by filing an annual Form 8996 with income taxes. That entity's organizational charter must also specify it is doing business in an Opportunity Zone. The sub- of its tangible assets be held in QOZ property.
- If the QOF doesn't meet the asset test of 90%, it pays a 5% interest penalty on the shortfall. If the sub-fund fails to meet the 70% asset test, it immediately is disqualified.

- An entity declares itself a QOF by filing an annual Form 8996 with income taxes. That entity's organizational charter must also specify it is doing business in an Opportunity Zone. The sub-fund entity isn't required to file a Form 8996, or to specify a purpose.
- At least 50% of a sub-fund's gross income must come from an active trade or business within the QOZ; QOZ working capital can count as qualifying income. QOFs are not held to that 50% rule, and can't use working capital as qualifying income.
- Less than 5% of a sub-fund's assets can consist of investment/intangible property — stock, partnership interest and debt — other than QOZ working capital. This is not the case with a QOF.
- Liquid assets can count as a sub-fund's property, as long as a written plan and schedule are in place to meet the 100% of cost test. Again, this is not the case with QOFs.

Lesson 3: Due Diligence

Due diligence is required for any investment; this is especially the case for QOF and sub-fund investments. Complicating the issue is that the Opportunity Zone program is still so new. Still, the following can help protect those investing in QOFs and sub-funds:

- Take note of the QOF's and sub-fund's structure and holdings. Both must pass the requirements mentioned above.
- Though sub-funds are not required to state their purpose, their holdings must be consistent with guidance.
- Keep an eye on the calendar; QOFs and sub-funds must pass an asset test every six months. Additionally, QOZ properties in which a QOF/sub-fund invests are required to be "substantially improved" within 30 months.
- Work with those who know what they are doing. At Greenberg Glusker, we have staff solely dedicated to understanding guidance and rules pertaining to the Opportunity Zone program. It's important to have access to expertise like this, to protect your investments.

While the Opportunity Zone program can provide positive benefits, it is still very new. This is especially the case for Qualified Opportunity Funds and their sub-funds. As such, an understanding about the investment and requirements is extremely important.

Module 2 Quiz: 3 questions

Module 3: COMMUNITY INVOLVEMENT AND OPPORTUNITY ZONES

- Capital that is funneled into Qualified Opportunity Funds can also provide ample opportunity for cultivating human capital for redeveloping inner-city and lower-income neighborhoods.
- Bringing talented minorities into commercial real estate deals can help boost understanding of local markets and business practices.
- Gentrification is a concern when pouring billions of capital gains into lower-income and economically disadvantaged areas.
- The highest number of gentrified opportunity zones are located in Rust belt metros, including Baltimore, Chicago, Detroit, Philadelphia and St. Louis.
- Opportunity zones in tech hubs and hotspots are experiencing high rates of gentrification.
- Many of the least-gentrified O-Zones are in Sun Belt cities.
- Of the top 100 most gentrified Opportunity Zones, 75 are within urban areas.

RCLCO Real Estate Advisors' Eric Willett (Vice President) and Brett Dunlavey (Analyst) opted to put numbers to the issue by identifying census tracts with the most gentrification in recent years. The researchers did this by examining changes in real estate investment, household income levels and associated demographic characteristics, from which it built a Gentrification Index. That index, in turn, was applied to every Opportunity Zone in the 25 largest metropolitan areas.

Here are some of the findings, issued in a report.

- ***Rust belt cities have the highest number of gentrified Opportunity Zones***. The report noted that 49 of the top 100 most gentrified Opportunity Zones were in Rust Belt metros, which included Baltimore, Chicago, Detroit, Philadelphia and St. Louis. Furthermore, "of the eight metros with the highest average gentrification scores, five are rust belt cities," the researchers wrote, adding that the findings show the regions' "comparatively overlooked neighborhood change and growing inequality."
- ***Opportunity Zones in new tech areas are experiencing high rates of gentrification***. The RCLCO analysts noted that, due to "high salaries, a disproportionately white workforce and increasingly urban campuses," O-Zones in metros such as San Francisco and Denver are experiencing higher rates of gentrification.
- ***Many of the least-gentrified O-Zones are in Sun Belt cities***. The RCLCO report pointed out that 55 of the 100 least-gentrified zones are in the Sun Belt cities, with different gentrification rates reflecting land use in these regions. One reason is because Sun Belt cities are, for the most part, suburban. Additionally, "the comparatively low barriers to entry and lower land prices in these metros create less pressure on local populations and fewer incentives for densification and reinvestment in contested neighborhoods," the report said.
- ***Gentrification is more common in urban neighborhoods***. Relocation of young, college-educated households into CBDs and urban cores has been a driver of gentrification. Of the top 100 most gentrified Opportunity Zones, Willett and Dunlavey said that 75 of those are within urban areas.

Overall, the RCLCO analysts found that the majority of the census tracts identified as Opportunity Zone-eligible, in that they are economically challenged. However, many of the tracts are located in more affluent communities. "We found 70 qualified Opportunity Zones in high-end neighborhoods . . . in which two out of three residents had a bachelor's degree or higher, and the current median income is $94,000," the report said.

Module 3 Quiz: 1 Minute

Module 4: ENVIRONMENTAL CONCERNS AND OPPORTUNITY ZONES

- How to choose sites for optimal business objectives.
- Once you have targeted some qualified Opportunity Zones for real estate development, your first objective is to evaluate how and if that parcel can accommodate your business objectives and potential building use.
- How to manage environmental and physical building risk.
- The U.S. Environmental Protection Agency recently targeted 149 communities to receive $64.6 million in funding for brownfield cleanup, almost three-fourths of which were Qualified Opportunity Zones.
- How to manage project completion and budget.
- The degree of success when investing in opportunity zones will depend on optimization of site selection for use and occupancy, understanding and pricing in all environmental and physical risks associated with the site, and ensuring timely construction progress and budget.

Lesson 1: Choosing Sites for Optimal Business Objectives

Once you have targeted some qualified Opportunity Zones for real estate development, your first objective is to evaluate how and if that parcel can accommodate your business objectives and potential building use. You must consider whether the location is optimal, if the site will require structural modifications, and whether the development is geared towards short-or long-term gains. Can you physically make your building work on the existing property? For example, will the space allow for an office, a mixed-use retail development or a logistics center for e-commerce goods? Will your proposed asset require a significant capacity, and can you provide the parking and access to make that work?

Before breaking any ground, start with a feasibility study to see what is actually possible. You might need a zoning exception for parking requirements, or a special permit for a business classification change if there is a specified zoning use for that area. Understanding the zoning requirements and what changes can be made “over the counter” without triggering a lengthy entitlement process, avoids delays and additional fees.

Lesson 2: Manage Environmental and Physical Building Risk

Be aware of the potential for environmental contamination, especially if your targeted property involves industrial, brownfield or long-abandoned assets. Indeed, the U.S. Environmental Protection Agency recently targeted 149 communities to receive $64.6 million in funding for brownfield cleanup, almost three-fourths of which were Qualified Opportunity Zones. To determine the extent of these contamination risks and liabilities, you will need to invest in an environmental assessment by an experienced consultant. Should the presence of environmental concerns be discovered, a remedial cost estimate plan can help you price in the cost of cleanup and provide guidance for state and federal regulation compliance. An environmental consultant can navigate a range of remediation concerns, from vapor intrusion, mitigating contaminated soil or water, or the removal of an underground features such as storage tanks or abandoned oil wells.

For renovation or rehabilitation of older buildings, it is wise to test for asbestos and other hazards such as lead paint and mold before and/or during construction.

If you plan to repurpose or renovate an existing building, a Property Condition Assessment (PCA) report will provide in-depth understanding of any necessary repairs or replacements, and the remaining useful life of the building’s systems. Big-ticket items like roofing, floors, and MEP (mechanical, electrical, and plumbing) systems must be assessed for capital planning. One of the distinguishing elements of Opportunity Zone investments is that you must improve the asset – often spending a significant amount of money – to qualify for the tax incentives. The PCA will provide a detailed opinion of costs for capital expenditures and immediate repairs necessary for transforming the asset and can even identify those items where your budget is best spent, to help you plan ahead for investment return.

If your Opportunity Zone asset is also located in a seismic zone, then certain developments or changes of use may necessitate seismic reinforcement or retrofitting to ensure building safety. Consult with a seismic expert to perform a seismic risk assessment. Engineers can help determine conditions and a scope for seismic strengthening, depending on your risk tolerance and use designation.

Lesson 3: Manage Project Completion and Budget

Whether you choose to pursue a ground-up development Opportunity Zone or rehabilitate an existing asset, your Opportunity Zone project will involve some form of construction services. If not managed properly, rising costs of construction and a persistent labor shortage can drain the profit from even simple renovation projects and increase the likelihood of contractor failure or a default. Therefore, construction risk management is an important tool in managing cost and minimizing delays or defaults, particularly for projects where cost savings are priced into the return on investment.

Even when pursuing the most exciting Opportunity Zone developments, be wary of rushing a project on the front end or hiring general contractors that are overbooked or are developing projects outside their realm of expertise. Sometimes, renovation projects can incur even more risk than ground-up development because you don't know what you are dealing with until you start demolishing and opening up structural elements. In these cases, making sure that the original budget is accurate and has enough contingency built in for any unanticipated costs is key. You can minimize these risks with construction risk management oversight measures, such as a pre-closing document and cost review, contractor evaluations before hiring staff, monthly progress inspections, budget monitoring and funds control to ensure contractors and vendors are paid on time.

Opportunity Zone incentives are an attractive avenue to pursue your investment objectives in a challenging market, at least until the program expires on December 31, 2026. Your degree of success will depend on optimization of site selection for use and occupancy, understanding and pricing in all environmental and physical risks associated with the site, and ensuring timely construction progress and budget.

Module 4 Quiz: 3 Minutes

Module 5: ENVIRONMENTAL CONSULTANTS

What should a real estate investor consider when choosing an environmental consultant?

1. Joseph Derhake outlines what an investor should look for when choosing an environmental consultant.
2. A number of environmental consulting firms specialize in other things but will do an ESA if asked.
3. ESAs are often relied upon by multiple parties. There is a benefit to choosing a firm that is credible with a number of different stakeholders.

Transcript of Video:

Joseph Derhake [00:00:11] Well, sure, there's a lot of environmental consultants out there and a lot of them are good, but, you know, some of them are not as good. Some of them really aren't committed to the field, there's alot of consulting firms that maybe really specialize in something else but will do an environmental consultant, if asked, will do a phase one environmental assessment if asked. So I would look for the most basic qualifications to be a environmental professional, which has a certain education and experience requirements. You might look for somebody that's registered like a registered geologist, or a registered professional engineer, is a safe choice. And you might want to be registered in the state in which you're working in or investing in. And then and then the one thing I would - this is a somewhat self-serving answer because we're a national firm and with a very big practice. But I think that the environmental site assessments are often relied upon by multiple parties. So a buyer is ordering it. But then that buyer will flip the report to their lender and they may even flip it to some sort of limited investor. And so there is a bit of a benefit when you choose a firm that is credible with lots of with lots of stakeholders and in some of the larger firms like us would meet that standard. And that if you flipped it to a lender to be named later, it's likely that our report would be accepted. And we do see a lot of times where people are kind of forced to repeat an environmental site assessment. And that's a really kind of a bad deal for them having to do, too, in a short period of time just because the first firm wasn't on some approved list of of some lender or capital provider.

Module 5 Quiz: 1 minute

M6: BEYOND THE BIG 4: DIALED IN DUE DILIGENCE FOR CRE ACQUISITIONS

When considering pre-acquisition property due diligence, many savvy investors request the "Big Four": Phase I Environmental Site Assessment (ESA), Property Condition Assessment (PCA), ALTA Survey, and Zoning Compliance Report. However, multiple complimentary services are available to help an investor, property owner and/or lender assess potential risk. Depending on the unique features of the property, as well as the buyer's anticipated use of the property, the Big Four core services may be supplemented with additional evaluations.

Some of these additional assessments will be driven by the location of the property. For example, properties located in seismically active areas, such as those on the west coast of the United States, may warrant a seismic risk assessment. For areas of high potential radon concentration, a radon survey would be beneficial. Properties that do not have a connection to public water and sewer services may require a drinking water evaluation to screen for lead in drinking water, as well as a septic assessment.

For properties where extensive renovations and/or demolition is planned, a hazardous materials building survey that evaluates the potential for asbestos containing materials, lead based paint, PCBs in caulk, mercury containing devices, and other materials that would require special handling and disposal would be informative. Similarly, for properties where potential development is intended, a wetlands and flood plain evaluation should be considered. An environmental lien search to identify Activity and Use Limitations (AUL) and land use restrictions can also yield valuable information pertaining to the property and potential development challenges.

Acquisitions during the coronavirus pandemic may warrant additional assessments as well. At the onset of the pandemic, many buildings were unexpectedly vacated for what was initially understood to be a short period of time but remained vacant for several months. If your target acquisition has been vacant for a prolonged period, consider an industrial hygiene evaluation to ensure that there are no leaking emergency generators or aboveground storage tanks, mold growth due to unbalanced HVAC and/or pipe leaks, or legionella blooms in water chillers. Solutions can be employed to swiftly and cost effectively address these conditions. As we proceed through the economic impacts of the global pandemic, there may be an increase in foreclosure activity. It may be prudent to conduct a regulatory compliance review pre-foreclosure. Should larger environmental issues be identified, a remedial cost estimate and remedial action plan will be developed.

For a potential property owner who wants to ensure appropriate conditions for future occupants and/or tenants, an Indoor Air Quality (IAQ) evaluation can be illustrative. Currently, there is an increased focus on industrial hygiene in commercial properties, primarily driven in response to COVID-19. Many commercial spaces are undergoing deep cleaning. Property owners may want to perform an IH cleaning evaluation on a regular schedule to provide confidence to their occupants.

With so many factors involved, developing a due diligence strategy requires thorough understanding of what tools are available and when to deploy them. You may find it helpful to use a due diligence checklist. Work with your due diligence consultant to develop a risk mitigation protocol that incorporates your business objectives and your level of risk tolerance, as well as the specific attributes of your target acquisition.

MODULE 6: QUIZ - 1 minute

MODULE 7: PHASE 1 ENVIRONMENTAL SITE ASSESSMENT
Lesson 1: Definition

A Phase I Environmental Site Assessment involves a careful review of all government, historical, and any environmental or other documentation related to the property in order to determine whether or not there are any contaminations to the property. This assessment should be performed by a professional environmental agent to ensure a quality review.

Lesson 2: Phase I 101

A Phase I Environmental Site Assessment, commonly referred to as an ESA, or Phase I ESA, is completed to research the current and historical uses of a property as part of a commercial real estate transaction. The intent of the report is to assess if current or historical property uses have impacted the soil or groundwater beneath the property and could pose a threat to the environment and/or human health. If these issues are found, it presents a potential liability for the lender and/or owner, as well as affecting the value of the property. A Phase I ESA completed prior to the closure of a real estate transaction can be used to satisfy the requirements of CERCLA's (Comprehensive Environmental Response, Compensation and Liability Act) innocent landowner defense under All Appropriate Inquiries (AAI).

Phase I Environmental Site Assessment reports can be completed on all types of properties including vacant land, agricultural, multi-family residential, commercial, and industrial uses; however, all Phase I ESA reports are completed to comply with ASTM E1527-13 (exceptions are made for properties comprised of large primarily undeveloped land, which can be researched under ASTM E2247-16).

A Phase I ESA typically includes the following:

• A site visit to observe current and past conditions and uses of the property and adjacent properties.
• A review of federal, state, tribal, and local regulatory databases including, but not limited to, underground storage tanks (USTs), aboveground storage tanks (ASTs), known or suspected release cases, the storage of hazardous substances and disposal of hazardous wastes including petroleum products, and institutional and engineering controls.
• A review of historical records, such as historical aerial photographs, fire insurance maps (Sanborn maps), historical city directories, and historical topographic maps.
• A review of state and local agency records, including but not limited to state environmental agencies, Building Departments, Fire Departments, and Health Departments.
• Interviews with current and past property owners, operators, and occupants, or others familiar with the property.
• Interviews with the Report User for title or judicial records for environmental liens and activity and use limitations (AULs); specialized knowledge or experience; actual knowledge; commonly known or reasonably ascertainable information; the reason for a significantly lower purchase price; and the reason for the preparation of the Phase I ESA. It is the User responsibility to provide this information to qualify for the innocent landowner defense.

This research is evaluated by the Environmental Professional (EP) to identify potential environmental risks to the property such as current or historic operations that are known or suspected to have used hazardous substances or petroleum products during onsite operations.

Common uses of concern are dry cleaners, gas stations, auto/vehicle repair, printing operations and manufacturing. In addition to potential soil and groundwater contamination, ASTM E1527-13 addresses the concerns associated with contamination in soil vapor and the potential for vapor migration to pose a threat to onsite and offsite tenants.

While not part of ASTM requirements, Phase I ESA reports typically include a discussion of observed suspect asbestos containing materials (ACM), potential lead-based paint (LBP) and mold growth; as well as the potential for lead in drinking water and radon. Sampling for these non-ASTM concerns is beyond the scope of a standard Phase I ESA but can be included upon request.

ASTM E1527-13 provides the guidelines for a Phase I ESA report to meet industry standard, but there are other factors to consider when ordering a report. Projects associated with Fannie Mae, Freddie Mac, U.S. Department of Housing and Urban Development (HUD), and the Small Business Association (SBA) each have their own report requirements. This is also true of other lending institutions.

Once a Phase I ESA is complete, the Environmental Professional will summarize what concerns were identified on the property and make recommendations about what actions, if any are needed to address these concerns. A recognized environmental condition (REC) indicates known contamination or the potential for the subsurface to have been impacted by contamination (either from the subject property or possibly from an offsite source). A controlled recognized environmental condition (CREC) identifies that the property has been impacted by contamination which has been investigated and remediated; however, contamination remains and would require additional work if redeveloped. A historical recognized environmental condition (HREC) identifies a release impacted the subject property which has been investigated and remediated meeting unrestricted use criteria.

The identification of a REC will often include a recommendation for a Phase II Environmental Site Assessment to collect soil, groundwater, and/or soil vapor samples from the subsurface to analyze for the presence of contamination.

Lesson 3: When to Perform one?

> Holly Neber [00:00:10] So a phase one ESA, an environmental site assessment, essentially tells the life story of a property, and from that life story, we draw conclusions about the potential for an environmental concerns at the site. Most of our clients use a phase one ESA to understand if there is an environmental impairment that might impact the value of the property, create a liability to the potential purchaser, or present a health risk to the occupants. So the life story of a property is really made up of three components. The first is the historical research, which consists of aerial photographs going back to the 40s, historical maps which can go back to the eighteen hundreds, the building permit history and historical occupancy records, etc. and that's the first section - historical research. The second is the current site conditions as identified during a site inspection of the property to inspect for the presence of hazardous materials and petroleum products and to see how those materials are stored and handled at the property if they're there. And then third is really a

regulatory status check on the property as well as surrounding and nearby sites. So with that historical research, the current site conditions and then this regulatory status check, we have a much better idea of what the conditions at the site might be presently. We follow the scope of work that's defined by the American Society for Testing Materials known as ASTM to document the history, current condition and the regulatory listings that I mentioned. And then we use that information to make a professional judgment about whether there are environmental concerns that, again, might either affect the value of the property, represent a liability to the purchaser of the property, or represent a health risk to the occupants. So we're hired to perform Phase Ones by prospective purchasers who want to kick the tires during their due diligence period and by owners prior to disposition who want to understand the current status before they market the property as well as by lenders.

Holly Neber [00:02:17] So why do the lenders want phase one? Well, lenders are looking at phase one essays prior to approving a loan on commercial real estate for a few reasons. Number one, they want to understand if the value that they're seeing in the appraisal is accurate. So if there is an environmental impairment worth, let's say, one hundred thousand to deal with, then that obviously would affect what affect the value of the property. So they're doing that as a value check on the collateral. They're also doing it because they want to avoid foreclosure risk if the borrower might not have the financial resources to deal with an environmental impairment that's identified. And then they also lastly want to avoid liability in the event they have to foreclose on the site. And that's both the liability of having to deal with the cleanup, the cost of the cleanup, as well as the reputational risk to the bank to be owning that site.

Joseph Derhake [00:03:07] The most basic level of phase one environmental side assessment tries to advise a real estate investor if there's any liabilities associated, any environmental liabilities associated with real estate asset. Specifically, it looks for recognized environmental conditions, which is a term of art, but it would cover uncover things like hazardous materials. And a lot of times these problems are the result of a property use that happened 40 years ago. In general, our society is smarter now than it was then with respect to environmental issues.

Stephanie Trueb [00:03:41] So a phase one environmental site assessment, also called an ESA is a report that's prepared for identifying potential or existing environmental concerns on a property. It's part of the due diligence for any type of commercial real estate transaction. It includes components like a site visit where we do a walk through of the property, we look at adjacent properties, we search regulatory databases, conduct interviews with people who are familiar with the property owners, occupants, previous owners. And we look at the history as well. When a phase one is performed, typically they're ordered by buyers, owners, lenders. Anyone really involved in a real estate transaction could benefit from a phase one.

Lesson 4: When does the need to perform one arise?

Transcript of Video

Holly Neber [00:00:10] So buyers and their lenders typically have a standard due diligence period within which a phase one environmental site assessment should be completed. Phase one's could be obtained at any time. However, users of these reports should be aware that certain elements will need to be updated after six months from the date of issuance. This is because site conditions can change. And so these phase one reports do have a shelf life.

Holly Neber [00:00:35] So a phase one, ESA typically takes from two to four weeks to complete, depending on the complexity of the project and the availability of records, both from the current property owner, the seller and the regulatory agencies. So it's really critical to begin the process as early as possible within your due diligence period and also to provide the consultant with all of the information you get up front so it can be incorporated into the research, particularly when concerns have been present in the past. Let your consultant know as early as possible so we can work through all the research that needs to be completed. So most people are kind of, they're navigating that due diligence period, making sure they're getting it done within that time frame. They're also looking at when they're going to receive the appraisal some time so they can compare the value to the environmental issues. And then also you want to make sure you don't do it too far ahead of time because there is a shelf life on it.

Joseph Derhake [00:01:28] So a phase one environmental side assessment typically takes three weeks for a standard turnaround. We routinely do them in two weeks and really can even compress a schedule further. You know, consultants will hustle. But the rub is, is that a phase one environmental site assessment requires to get certain information from the government. And so there's a limit as to how much you can expect governments to hustle. Sometimes some jurisdictions are really actually quite slow. And so as you can press inside of three weeks, you really run the risk of getting to the end with not one hundred percent of the information, but sometimes a phase one environmental side assessment will recommend a phase two investigation - where you go back and do some physical testing. And so if you want to develop a contingency period that allows for both the phase one and potentially a phase two. You know, you might allow six weeks if you did have the luxury of time. I realize that today's commercial real estate market, aggressive close times are coming.

Stephanie Trueb [00:02:34] So typically for a an owner or a borrower who's looking to get a loan, they would have a due diligence period, which is - it can range from 60 to, well, 30 to 60 days, really. And so in that time frame, they would order the phase one. And usually our turnaround time is about three weeks. Sometimes we do it in 10 days, but that gives them a time period for us to complete the phase one and then do any additional actions that may be recommended. So we are seeing recently that turnaround time being cut down more and more as people are trying to get their transactions done before the end of the year, so - the time frame varies.

Lesson 5: Phase 1 Assessment Legalities

Is it a legal/regulatory requirement to act on the recommendations of a Phase I assessment?

1. Holly Neber, Joseph Derhake and Stephanie Trueb discuss legal and regulatory requirements surrounding Phase I assessments.
2. In order to qualify as an “innocent land owner” under superfund law it is required to obtain a Phase I assessment.
3. Many clients are obtaining Phase I assessments simply as a matter of internal risk management and as an industry best practice.

4. Typically with a Phase I ESA you are not identifying an immediate health risk to the community so there are no reporting requirements.

Transcript of Video:
Joseph Derhake [00:00:10] Yeah, the short answer to that question is no, we're a consultant and we just provide a recommendation to our clients and to some extent the recommendation can even be adjusted to business circumstances. Just to tie this whole thing back to regulations is if you're buying a property, you would want to be eligible for the innocent land owner defense under CERCLA. And so conducting all appropriate inquiry is required for that defense. And the EPA has opined that a Phase one environmental site assessment does include all appropriate inquiry. Of course, if it recommends a phase two, then you may need to deal with that issue to actually qualify as this innocent landowner.

Holly Neber [00:00:58] So it depends. Of course, the answer is it depends. So generally speaking, Phase one ESA's are done for a number of reasons. As I outlined earlier, one of those reasons is in order to qualify as an innocent landowner under all appropriate inquiry, which is part of CERCLA law, which is also known as Superfund law, and so appropriate due diligence as defined under CERCLA law to become an innocent landowner is a form required within the phase one essay. So many clients are indeed pursuing all appropriate inquiry and innocent landowner status. However, many clients are obtaining phase ones simply as a matter of their internal risk management and as an industry best practice. And so if you're only doing it for internal risk management practices or an industry best practice, then you not necessarily have to act on that information. You may act on that information by not going forward with the purchase, by budgeting for certain environmental clean up requirements that may be needed. But typically with a phase one ESA, you're not gathering any data, you're not gathering soil samples, groundwater samples, you're not identifying an immediate health risk to the community. So there's no reporting requirements required with that.

Stephanie Trueb [00:02:17] So to act on the recommendations, it's not necessarily a regulatory requirement. Recommendations and phase one reports are really opinions of what the environmental professional thinks, a certain situation, how it should be handled. Occasionally what we recommend could be regulatory. For example, if a phase two was done and contamination was a found and it needed to be reported and the phase one may - and that hadn't been done yet, then the phase one might recommend something like that. As far as legal. I would say most lenders would typically want those recommendations to be done. It may be a requirement to get a loan. I know that for SBA loans, for example, any recommendation in their environmental due diligence has to be completed typically before the loan closes.

Lesson 6: Recommendations for Phase I
Do you have any recommendations for people ordering Phase I ESAs?

1. Holly Neber gives her recommendations for buyers and landowners ordering Phase I ESAs
2. Phase I ESAs are done for a particular user at a particular time. Using older Phase I reports from a previous buyer or landowner is not ideal.
3. If using an older report, it is recommended to get reliance on that report from the original reporting consultant.
4. In the case of a redevelopment, it is recommended to disclose plans (What type of disturbance to the site? Will there be a basement?) for the site to the consultant.
5. If there is a concern with the property, your consultant should explain it to you and you should be able to understand.

Transcript of Video:
Holly Neber [00:00:12] It's important to know that phase one ESA's are done for a particular user at a particular time. So while it might be tempting to rely on an older report and you definitely should review them, it's also important to get fresh eyes on the site with your particular needs in mind. If you do want to use someone else's phase one and older report, you'll want to try and get reliance on that report from the original consultant and you'll want to be aware of any potential conflicts of interest, and definitely the insurance coverage is held by that consultant. Also, if you're conducting the phase one ESA for a loan, you'll want to make sure the consultant you're using is approved by the lender and understands the lender's scope of work. Many lenders add scope of work items to the phase one, such as asbestos, lead based paint, radon that type of thing. So in addition to making sure your consultant understands the scope of work, make sure they're approved by the lender.

Holly Neber [00:01:09] Also, things like checking the radon zone or the flood zone are not required by the ASTM standard, but they are optional to include. And one thing we're seeing more of these days is clients asking for us to include climate change risk within the phase one physical conditions that we're checking. So you can always talk to your consultant about what the add ons might be to your scope of work, depending on what your needs are. So, again, make sure you convey the purpose of the assessment to the consultant, fully understand the scope of work, make sure it meets your needs. There's a difference between getting a phase one just to complete a property transaction or get a loan versus getting a phase one because you're redeveloping a brownfield site. In the case of a redevelopment, you'll want to really share the plans for the redevelopment. Are there a lot of subsurface features planned as they're planning to be, a lot of grading happening? Are there going to be basements? What type of disturbance is planned for the surface of the property? You want to make sure that your consultant can overlay the proposed development plans with the environmental conditions that might exist at the site. And the most important recommendation I would have is that if there is a concern with your property, you should feel totally comfortable and that you understand that your consultant should explain it to you. It's really not rocket science. We are scientists, engineers, geologists. But this is still something that should be totally understandable by the layperson. It's essentially a health check on a property based on the property's life story. And it should be easily understood. If you have trouble with the findings, you just don't feel like it makes sense or it doesn't sound right to you. We really recommend people reach out and get a second opinion, just like you would with a medical diagnosis. It's OK to run things by other experts, get a diversity of opinion on things. And especially when you have impairment and you're looking at mitigation in the context of redevelopment, especially, you may want to reach out to several different experts and get their thoughts on what would they recommend and next steps, what would they recommend for budgets and ask for their resumé on what types of sites have they worked on with similar issues? And what kind of relationships do they have with the regulatory agencies in place, especially with redevelopment projects where you have open cases, open releases, there's regulatory agencies, there's case managers involved. If you're working with a consultant that knows those folks, it can really help to help the process move forward smoothly. And then just in general, the best consultants are trusted advisers that are there to help you achieve your goals, and that is by helping you have access to information so you can make an informed decision. That's my recommendation.

MODULE 7: QUIZ - 5minutes

MODULE 8: PHASE II ENVIRONMENTAL SITE ASSESSMENT

Lesson 1: Definition

A Phase II Environmental Assessment occurs if a Phase I Assessment reveals the possibility of contamination on the property. To determine the extent of the contamination, soil and other samples are taken and subjected to specific laboratory tests.

Lesson 2: Phase II 101

When a Phase I Environmental Site Assessment (ESA) identifies a recognized environmental condition (REC) or the potential for impacts to the subsurface at a site, most clients request to evaluate the potential impacts by performing Phase II Environmental Testing. The presence of a REC or an environmentally-impacted property can greatly reduce its value. Stakeholders want to reduce liability and future cleanup expenses on their investment by conducting a Phase II ESA, in which a subsurface investigation tests soil, soil gas and/or groundwater to identify sources of environmental impacts.

If a buyer or lender doesn't have a full scope and realistic picture of a seemingly limited REC, they could be leaving themselves exposed to hidden risk. The Phase II ESA can limit this risk and, in many cases, it can also protect against substantial long-term costs and complex environmental liabilities.

The purpose of a Phase II Environmental Site Assessment Report is to evaluate the presence, or absence of, petroleum products or hazardous substances in the subsurface of the site. A trained, licensed, experienced staff of geologists and engineers that possesses expertise in Phase II Environmental project design performs these assessments per the ASTM E1903-11 Standard Guide.

ASTM E1903-11 provides some basic parameters for Phase II Environmental Assessments, but there is a huge amount of professional judgment that goes into the final report. A lot more goes into the scope of work than just the number of samples taken – for example what type of drilling and sample collection is appropriate for the site and the kinds of contaminants you are looking for. That's why it pays to engage an informed, experienced due diligence consultant who understands what's involved in the assessment and the level of certainty your institution requires.

When designing a Phase II ESA scope, the environmental professional accounts for any areas of concern, chemicals of concern, local geology and/or site access issues as well as local, state and federal regulations. An accurate, helpful Phase II ESA delivers local knowledge of geologic and regulatory environments, and then interpreting geological and chemical data to the client so that they are fully informed of their business risk.

Drilling methods used most often by scientists and geologists during Phase II Environmental Testing projects include:

- Push Probe
- Hollow Stem Auger
- Hand Auger
- Mud Rotary
- CPT Drilling

Lesson 3: When to perform one

What leads to a Phase II assessment? What types of situations typically involve a Phase 2 assessment?

1. Holly Neber, Joseph Derhake and Stephanie Trueb outline the circumstances that may lead to a Phase II assessment.
2. A Phase II would be recommended when a Phase I assessment identifies a concern that warrants further evaluation.
3. In a Phase II actual soil samples and water materials are collected.
4. Typical red flag uses include: Dry cleaners, gas stations, auto repair facilities and industrial uses like printing and manufacturing… etc

Transcript of Video:
Stephanie Trueb [00:00:10] So what can lead to a phase two quite commonly is historical use, like if we find out that there's historical manufacturing in a property, historical industrial use, gas stations can present a concern. Underground storage tanks that may be older. They could have leaked any type of spill that we see while we're out on site. If we think that it could have impacted the soil or the groundwater, the subsurface, then we might recommend a phase two. Dry cleaners - they can be a pretty significant environmental concern for which a phase two might be warranted.

[00:00:58] So a phase two would be recommended when the phase one identifies a concern that requires further evaluation. So the phase one is strictly a research project. There's no intrusive sampling of any kind. And unless it's added to the scope, so a phase two is where we actually go out and collect soil, soil vapor or groundwater samples to see if the concern that was identified in the phase one actually resulted in an impact to the property. So an example would be, let's say a phase one identifies in the historical records that a dry cleaners was present at a retail center from, let's say, nineteen seventy to two thousand. That period of time gives us reason to suspect there may have been a release to the subsurface of the property from the dry cleaning business. So we recommend to phase two and in the phase two stage samples would actually be collected of the soil, soil vapor and typically groundwater as well, depending on how deep groundwater is. And then the samples are then analyzed for dry cleaning chemicals to see if because of the history of use, there is an actual impact to the property. So it's a lot like going to the doctor, getting a doctor visit where they're concerned about something and they ask you to do some lab work so that the phase one is the doctor visit - and the phase two is the lab work. So in the second part of your question. Typical red flag uses, in addition to dry cleaners, include gas stations, auto repair facilities and industrial uses such as printing, plating, circuit board manufacturing and other types of manufacturing. So the longer the site history and the more industrial the area within which the site is located, the more likely we are to see these types of uses having occurred either on the property or within the surrounding area. And it's important to note that even if the subject property hasn't had an occupancy of concern, a nearby site can result in a subsurface impact to a property. So contamination plumes within soil vapor or within groundwater can travel hundreds of feet, thousands of feet, in some cases even one to two miles. So these types of plumes represent a potential risk to occupants of the property, even if the release of the chemical didn't happen on this property. So on occasion, we're also performing phase two is to assess whether an off site release might be causing any type of health risk to the occupants of the property, because certainly that also represents a liability to subject property owners as well as a potential impairment of the value of the property.

Joseph Derhake [00:03:33] So we probably we recommend a phase two in less than 10 percent of the phase one's we do, but what would happen is there would be some use of the property, often a long time ago that they operated, they used hazardous materials and maybe they would use the hazardous materials in a period of time where there was very little regulations. And so we rightly point out that there's some percent chance that that hazardous material was released to the subsurface soils or even maybe to the groundwater. And then we would recommend to figure that out, to figure out if it actually is there or not in a phase two environmental site assessment. And that would involve geologists coming back and and drilling holes, taking soil samples, maybe soil gas or groundwater samples and running them to a laboratory.

Lesson 4: Phase II Assessments and Brownfield Sites

Are we likely to see more Phase 2 assessments occurring as more brownfield sites are acquired for development or redevelopment?

- Holly Neber, Joseph Derhake and Stephanie Trueb discuss brownfield sites and the likelihood of Phase II ESAs needing to be completed there.
- Brownfield sites are more likely to have long and complex industrial histories or be situated in areas with those type of histories. In this situation, a Phase II is more than likely warranted.
- As real estate markets get hot, developers are going back and dealing with properties that have issues like solvents in the soil because it is worth it.

Transcript of Video:
Holly Neber [00:00:12] Yes, certainly brownfield sites are more likely to have long and complex industrial histories or be situated in areas with such histories, and these types of sites often require Phase Two's. So that much is true. The good news is that with a good Phase Two comprehensive scope of work, we can ultimately quantify the likely range of cost scenarios involved with addressing the concern. And then it simply becomes a math problem of how do you cover those costs within the redevelopment plan and how do you incorporate the mitigation strategies throughout the development plan. So there are solutions to all these environmental concerns. And honestly, as consultants, our proudest moments are when we tour a site that's been redeveloped and we've been part of taking something that was a blighted, difficult area, and has been become a great part of the community as a result of the clean up actions that have happened there. So we love contributing transformations and it's all it's all possible with the right planning in place from the beginning.

Stephanie Trueb [00:01:18] Quite possibly, I could see an uptick in the number of Phase Two's that are conducted and people are saying the tax benefits on these brownfield's as they're being redeveloped, they typically would need an investigation to determine if there's any contamination so that they can properly address it either through remediation, the clean up or managing it in place during development.

Joseph Derhake [00:01:48] Yeah, sure. So if you're buying a brownfield, you you know, you're buying a vacant property that had previous use and perhaps industrial use, you know, in a part of town where, you know, it's all been developed around it often and this area has been left vacant. And so, you know, the implication is that there is environmental problems, but not necessarily. It just really depends on the past use clearly. Like, if you're you know, there's a lot of past uses that would not at all need a phase two. And but, of course, in industrial use or any kind of use in petrochemicals or solvents would necessitate a phase two. And then you see that a lot as the real estate developer, as real estate markets get hot, that people are going back and dealing with property properties with problems because it's worth it.

Lesson 5: Phase II Challenges

What challenges might arise when there is a need for a Phase Two?

1. Stephanie Trueb discusses the challenges that arise during a Phase II assessment.
2. A lot of lenders don't want the sign the engagement for a Phase II because there is liability involved with going out to the property and drilling.
3. More often over the past several years, lenders are requiring borrowers to engage consulting firms for Phase II assessments.

Transcript of Video
Stephanie Trueb [00:00:11] A lot of lenders don't want to sign the engagement for doing a phase two, there's liability involved because we're actually going out onto the property and drilling.

Stephanie Trueb [00:00:23] So there's also implications in regards to CERCLA liability protections. The lender doesn't want to be seen as managing any type of environmental investigation or cleanup at the property. So - we are seeing more and more over the past several years that lenders are requiring their borrowers to actually engage us for phase two's.

Lesson 6: WHEN IS A LIMITED PHASE II ESA CALLED FOR?

There are circumstances in the due diligence process when a potential property owner does not want to invest in a full Phase II ESA. They may instead opt for a limited Phase II sampling, which is conducted to confirm the presence of a pollutant and may be limited by locations sampled, number of samples, media sampled or a combination. A buyer may conduct a limited Phase II ESA to evaluate the following scenarios to inform their transaction decisions:

●The identified REC from a Phase I ESA is minor or limited in scope
●To confirm a REC that presents more of a risk than the buyer is willing to accept
●To identify a REC that requires more discovery (a full-scale Phase II ESA) to confirm the extent of contamination

MODULE 8: QUIZ - 4 minutes

MODULE 9: OPPORTUNITY ZONES MYTHS AND QUICK FACTS

Lesson 1: Misunderstandings

Even as billions pour into Opportunity Zone funds, misconceptions persist on what exactly the Opportunity Zone program entails. "It is a great program that should pull capital into under-invested areas," said Darryl Jacobs, co-founder of law firm Ginsberg Jacobs in Chicago. "But to get the most out of the program, investors must do their due diligence.

“Deals still must pencil out,” he added. “Investors also need to make sure they understand the program’s rules, or they may fail to get the hoped-for tax deferrals or breaks or, even worse, face penalties.”

Jacobs cited—and corrected—five common misunderstandings about the Opportunity Zone program:

- All capital gains qualify. The gains must arise from a sale between Dec. 22, 2017 and Dec. 31, 2026, and must be invested in a Qualified Opportunity Fund (QOF) within 180 days of the gain recognition date.

Furthermore, “if you own a property in the Opportunity Zone, you can sell it to anyone, but not all buyers will be eligible for the tax advantages,” said Jacobs.

- Capital gains can be deployed at any time before 2027. In fact, a QOF must deploy 90% of its assets into eligible property within six months of the fund’s designation or Dec. 31 of the year in which the fund is formed, whichever comes first.

- All money in a QOF has to be invested in the Opportunity Zone. In fact, as little as 63% of the fund can be invested in qualifying assets, depending on how the fund is structured. That’s under the “70-30 rule” included in IRS guidelines issued last October.

- Any existing building in an Opportunity Zone qualifies. Properties must be newly- constructed or “significantly rehabbed” within 31 months. The property may be commercial or residential, but can’t be a “sin property,” such as a liquor store or massage parlor.

- Investors pay no taxes on capital gains after 10 years. Assuming the investor makes an investment in a QOF prior to Dec. 31, 2019, he or she is allowed to defer paying taxes on the original capital gain—i.e. the money invested into the QOF—until divestiture or Dec. 31, 2026, whichever occurs earlier. However, since the original gains are taxed no later than Dec. 31, 2026, an investor needs to invest gains no later than Dec. 31, 2019, to get the maximum tax benefit.

“The longer an investment is held, the more tax benefits the investor reaps,” said Jacobs. “And if they’re willing to commit a decade or more to a particular project, they are rewarded for the risk they take in the form of tax-free gains—but only if that project is successful.”

Lesson 2: ABCs of Opportunity Zones

What is a Qualified Opportunity Zone? In 2018, state officials designated areas under the poverty level, that required gentrification. Congress evaluated these selections, approving approximately 8,700 zone areas throughout the country.

What is a Qualified Opportunity Fund? A QOF is a corporation or partnership that invests in a QOZ and can include LLCs taxed as partnerships.

What gain qualifies? Any gain taxed as a capital gain generated from a sale with an unrelated party qualifies. If you invest the equivalent amount of any capital gain in a QOF, the investment will qualify. Keep in mind that if you invest only part of your gain, then that is the amount that will qualify for the benefits.

Who can elect to invest gains in a QOF? Any individual or entity can elect to defer the gain and invest it into a QOF. In the case of an S-corporation or partnership (including LLCs taxed as partnerships), the entity can elect to defer the gain, or can pass the gain out to its partners or shareholders, which then can elect to defer their portion of the gain.

When do I need to make the QOF investment? You have 180 days from the time of the gain in which to invest in a QOF; this includes weekends and holidays. During the 180 days, you can do anything with the money. Unlike a 1031 exchange, the money does not have to go to an intermediary. If the gain is flowing to a partner or a shareholder from a partnership or corporation, the individual has 180 days from the end of the entity's tax year in which to invest in a QOF.

How does a corporation or partnership become a QOF? The entity must add a Form 8996 to the tax return when filing. Yes, it is that simple.

How does one elect to defer the gain? The individual or entity files a Form 8949 with an income tax return for the year in which it elects to defer the gain.

What does a QOF do with the money? The QOF must invest the gain money, or allocate 90% of it, into a QOZ project within 180 days from the date it receives the funds.

What can a QOF invest in? A QOF can invest in property to be developed, stock in a business or partnership interest in a business or development, as long as the investment is in a QOZ.

What is a QOZ-qualified business? At least 50% of that business' gross income must be derived from the active conduct in the QOZ. Additionally, substantially all business-tangible property must be in the QOZ. Less than 35% of its property — such as stocks — can be in non-qualified property.

What businesses do not qualify? "Sin businesses," such as a country club, golf course, massage parlor, suntan facility, gambling facility, hot tub facility, racetrack or any business that its principal business is the sale of alcoholic beverages off premises do not qualify.

Will I still pay tax on the gain if I invest in a QOF? Yes. Tax on the capital gain deferred will be paid in 2026, regardless of when the gain was recognized. If you hold the QOF investment for five years by 2026, you will pay tax on 90% of the gain. If, by 2026, you've held the investment for seven years, you will pay 85% of the gain. The gain will be based on the original classification.

Can I invest other money in a QOF and get the benefits of the program? No. Only deferred capital gains qualify for the benefits.

What are other benefits? The program's best benefit is that, if you hold your QOF investment for at least 10 years then sell it, you can elect to step your basis in the QOF investment up to fair market value. This means you would pay no tax on the gain from the QOF investment.

MODULE 9: QUIZ - 1 minute

Thank you for completing the Connect Classroom's Opportunity Zones: Commercial Real Estate Investing and Environmental Site Assessments Course!

Please complete the following exam to receive full continuing education credit. You will be able to take the exam twice and must have a 70% score to pass.
Once you have successfully passed the course exam, you will be directed through the process to receive your certificate.

QUIZ DIRECTIONS
Quiz questions are multiple choice or true/false. Choose the best answer. You will have 1 opportunity to answer the questions. Correct answers allow you to move forward in the course.

FINAL EXAM
Please complete the following exam to receive full continuing education credit. You will be able to take the exam twice and must have a 70% score to pass.
Once you have successfully passed the course exam, you will be directed through the process to receive your certificate.

Before we take the final exam, let's check that we have all of your information correctly logged on file -- this is important as it'll be used on your certificate! -- Here's what we have on file for you:

First Name:

Last Name:

Unique ID:

Professional Number:

If any of this information is missing or incorrect - STOP NOW! - and update it first in your My Account Page.

Verify that your name matches the name below. Enter your name and today's date, then click "continue" to begin.

Thank you for completing the Opportunity Zones: Commercial Real Estate Investing and Environmental Site Assessments Course!

Please complete the following exam to receive full continuing education credit. You will be able to take the exam twice and must have a 70% score to pass.

Once you have successfully passed the course exam, you will be directed through the process to receive your certificate.

10 questions, 1 minute each question, 1 minutes total = 10 minutes to complete

Prior to taking the examination, please fill out our identification confirmation form and enter your DRIVERS LICENSE

To confirm your identity please type in your state-issued drivers license or government-issued identification.

Verify that your name matches the name below. Enter your name and today's date, then click Start Exam to begin. While taking this exam, please ensure that you are in a private room to avoid distraction with a stable wi-fi connection. Once you begin the exam you will be unable to pause it or restart it. If you do not pass within 1 attempt, the course will need to be retaken.

I, NAME, certify and ensure that by written statement signed under penalty of perjury that the participant enrolled is the person completing the course."

Type your name and the date to certify your identity