ENVIRONMENTAL LAW

Liabilities of Lenders

GLEN SMITH

Corrs Chambers Westgarth, Solicitors, Brisbane

INTRODUCTION

Greg Pearce in his paper has provided us with a comprehensive overview of the present state of the law and suggests some very sensible means by which a financier can put in place check lists so as to be able to identify high risk properties or high risk business operations.

FURTHER PRACTICAL PROBLEMS

My experience has been that, to a great extent, that is when the hard part starts. Having identified that you are dealing with a high risk property or a high risk business operation the question that the financier then confronts is what exactly should be done.

In the case of an experienced environmentally aware operator of long-standing, it is much more likely that suitable environmental management programmes will already be in place. In such a case, all that may be necessary is for the financier to be provided with details of those programmes and for the financier to then consult with its experts to confirm that the environmental compliance programme is satisfactory.

In other cases, where a new environmentally unaware operator is involved, there is likely to be an initial problem in that the financier in many cases may need to convince its customer of the need to put in place some suitable environmental management plan in relation to its business. That type of supervisory role has not been the traditional role of a financier. Clearly, the ultimate incentive for borrowers to put in place proper environmental compliance programmes is the fact that it is likely in the future that they will not be able to obtain finance unless they have done so.

CHECKING THE EXPERTS

A further practical difficulty is that even if a financier is presented with details of an environmental audit and an environmental compliance programme, that may not be sufficient. It will be cold comfort to a financier to have received a copy of an environmental audit and an environmental compliance programme if, at the end of the day, the audit is not satisfactory or the programme is deficient. In such a case, the value of a security property may still be reduced due to contamination. Alternatively a customer may lose a licence required to carry on its business and thus become unable to service its financings. Financiers will need to satisfy themselves that the terms of reference, methodology and conclusions adopted in respect of an environmental audit and in relation to compiling an environmental compliance programme, are appropriate to ensure compliance with legislative requirements. A secondary question also arises as to whether the appropriate experts have been engaged in preparing the audits and compliance programmes.

EXPERT NETWORK

Leading from that matter is the issue of exactly where a financier goes to seek appropriate confirming advices.

At the present stage, there is a growing network of technical experts available with particular areas of expertise; for example there are companies that specialise in the remediation of service station sites and others in the remediation of mining sites. It seems, from discussions with environmental lawyers, that the network of experts in this area is still in a somewhat embryonic stage.

At this stage, financiers may have difficulty in being able to easily establish the identity of the expert most appropriate to the particular industry or remediation problem. In the short-term, the task of being able to identify the appropriate expert may, in itself, prove to be a time-consuming and administratively burdensome exercise for financiers.

RISK EVALUATION PROBLEMS

In cases where a financier receives an environmental report which highlights potential risks, the next problem for the financier is how to place a value on the potential risk for security adequacy purposes.

In some cases, the report may make this a relatively simple exercise. In many cases, however, it may be extremely difficult. The problem is that the potential costs of remediation are subject to extreme variations. For example, I understand that the costs of remediating a service station site generally range from approximately $20,000 to $200,000. In a case where security over a service station site is involved, it is therefore imperative that a specific report be obtained on the specific security property and that a financier would be imprudent in these cases to rely upon average remediation costs.

For example, in a case where a business has some potential for polluting adjoining properties by means of the escape of contaminating fluids, it is extremely difficult for expert reports to place a monetary value on the potential remediation costs. On that basis alone, a financier is faced with an extremely difficult exercise in trying to determine the issue of security adequacy. This position is made even more difficult because any evaluation should also take into account the probability of pollution occurring. That probability should be assessed after consideration of the adequacy of measures taken by the business to prevent or minimise pollution.

In relation to small value transactions which involve a hazardous type of operation, it seems that the only prudent approach that a financier can take is to simply opt out of that form of lending unless the borrower is prepared to undertake a suitable environmental audit and to implement proper environmental due diligence programmes.

QUEENSLAND POSITION

In relation to the Queensland position, developments are still in a somewhat embryonic stage. With the forthcoming legislation it is anticipated that licences to operate potentially contaminating businesses, will have strict standards and guidelines with which many existing businesses will not be able to immediately comply.

In such cases, it is understood that businesses will be able to negotiate environmental management plans with licensing authorities to allow staged progress towards compliance. As part of such an environmental management plan it is expected that environmental audits will be required to ensure that businesses are meeting their obligations under the plans. Accordingly, in the future financiers may be able to use these plans and audits to satisfy their concerns both at the time of initially considering a lending proposal and also as a means of monitoring compliance during the currency of a loan.

I understand there are also proposals in Queensland for local authorities to have a supervisory role in respect of environmental compliance and standards at a local level. The concern in this matter is that there may well be divergences in the administration of standards from one local authority to another. This produces a consequential difficulty for financiers. In relation to any particular type of business, financiers will not be able to confidently rely upon the approach taken by one local authority as being indicative of the approach which may be taken by another local authority.

UNIFORMITY ISSUE

There is presently a considerable amount of uncertainty and inconsistency in the laws concerning environmental protection in Australia as they affect financiers.

A submission has been made by the Law Council of Australia, advocating the need for national uniformity in environmental protection laws in Australia as they affect financiers. Clearly, this can be achieved by means of either national or uniform state legislation. The submission also advocates that the liability of financiers should be limited to cases where there is actual fault on the part of the financier in polluting acts of the borrower. In other words, something going beyond the mere providing of finance or the taking of security over land which may be polluted or upon which hazardous activities may be carried out.

It seems to me, that those submissions are abundantly sensible.

I regret that my comments highlight a number of practical problems without offering any easy solutions. There are, however, in my view, no easy solutions.