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# Engineering and Environmental Reports

## Common Issues and Best Practices

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**High quality engineering and environmental reports help prevent credit losses**

### Key Takeaways

- Opportunities for improvement
- Selecting the best consultants
- Evaluating consultant reports
- What is expected from the consultant

## Common Report-Specific Issues

### Engineering

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- Too often certain problematic materials, such as polybutylene piping, are identified but the potential risk is not evaluated. To complete the risk assessment, the consultant needs to understand how long the material has been on the property, the common pitfalls with the material/installation of the vintage that has been identified (many materials that have a history of problems are modified over time so that each vintage has unique characteristics), and the maintenance experience at the subject property. Then the consultant can make a recommendation and price the alternative solutions as appropriate.
- In some instances, further study may be required before a final recommendation can be made. For example, while it may be impossible for the consultant to identify the specific resolution for an observation, such as building settlement, without further investigation they can usually attempt to bracket the range of typical causes and corrective actions (which allows them to bracket the potential cost), and they must note the time required and the cost for any recommended further study/testing.
- Adequate justification must be provided for any waiver requests. For example, we have a 60 amp minimum electrical service requirement; however, certain reports have noted existing 40 amp electrical service to be adequate without providing any supporting analysis. A load analysis must be provided along with confirmation that the local building authority takes no exception (e.g., no code violation due to this issue) before such a waiver can be considered.
- Costs to complete all work in progress must be identified and the time required for completion must be estimated. Freddie Mac must be able to tie the completion of such work to the loan terms.
- The reserve analysis should not be manipulated merely to produce a number that works with the underwriting analysis. The reserve analysis is intended to reflect the consultant's opinion regarding the remaining useful life of major building components; as such, the amount to be reserved for each component must reflect the remaining useful life of that component and not its expected useful life.
- All pending information must be provided in a timely manner.

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Please note that these best practices are not new requirements, nor do they replace existing requirements, but rather are applied, contextual support that complements the requirements of Chapters 12-14 of the *Freddie Mac Multifamily Seller/Service Guide*.

## **Environmental**

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- The required asbestos scope is often not fully addressed. Some consultants still do not consider the potential risk from asbestos due to the building age and/or do not test all suspect friable materials. Asbestos is still being produced and imported into this country, so there is no cutoff date that allows the risk analysis to be dismissed. Freddie Mac does not allow friable materials with concentrations above 10 percent to remain in place so all friable materials must be tested to determine the asbestos content.
- Recent changes to language in the *Freddie Mac Multifamily Seller/Service Guide* (Guide) have attempted to correct misconceptions regarding radon. We generally expect radon to be tested on every property. Radon concentrations are site specific and the risk cannot be adequately determined based on the EPA radon zones. The EPA specifically notes that the zone designations should not be used as a determinate in the testing decision. While there may be limited legitimate reasons that Freddie Mac will consider for waiving radon testing, location in a particular EPA zone is not among them. All elevated radon results require further testing and, in addition, the consultant must indicate the cost of potential remediation.
- A recommendation and cost estimate must be provided for any issue identified. For example, if the database search identifies a potential hazard at a nearby property, sufficient information must be sought so that a cost to cure can be identified. The consultant should discuss such situations with the client before issuing the report, as additional analysis (and consultant expense) may be required before the report is issued. In this case, the report could include a case file review and contact with the case manager to adequately understand the potential hazard.
- In certain cases, potential hazards cannot be fully evaluated without testing. For example, issues such as underground tanks with no historical test information or a dry cleaner with a documented spill, will likely require on-site testing to adequately evaluate the environmental risk before the report is issued.
- Costs to complete all work in progress must be identified and the time required for completion must be estimated. Freddie Mac must be able to tie the completion of such work to the loan terms.
- All pending information must be provided in a timely manner.

## **Best Practices**

### **Selecting the best consultants**

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- Evaluate and select consultants based on qualifications and quality of work — not strictly based on price or turnaround time
  - Qualify new consultants per Guide requirements
  - Ensure consultants are qualified, including on-site inspectors, and require that their resumes are included in the report appendix
  - Understand if sub-contractors will be used to perform the site inspection and, if so, how quality control is maintained



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- Ensure that consultant skills are matched to deals that require specialized knowledge
  - Include resumes of personnel used to conduct on-site analysis in the report appendix
- Ensure the consultant clearly understands the scope of work
  - If a new consultant, ensure they are familiar with the Guide chapter that describes work scope
  - The consultant should state the required scope of work in the report

### **Managing engagement**

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- Sellers should be interactive with consultants:
  - Convey Freddie Mac's requirements and your requirements and any unique aspects of the transaction to the consultant
  - Follow up with the consultant on any pending information identified in the report; this information must be submitted to Freddie Mac
  - Give feedback (positive and negative) to consultants in a timely manner
  - Encourage borrowers to provide historical property information including recent repairs, planned improvements, and any past third-party reports
- Consultants should be interactive with the Seller:
  - Understand who on the Seller's team is using their reports and communicate directly with those individuals
  - Convey any unique aspects of the property
  - Convey industry trends

### **Evaluating reports**

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- As required by the representations and warranties, fully review reports to confirm scope and verify issue resolution before submitting to Freddie Mac
- Ensure all issues are resolved before closing deals
  - Generally, it is not appropriate to require testing or further investigation after closing as problems (and required costs) could significantly exceed expectations
- Keep track of consultant performance, aggregate results from multiple report reviewers, and share performance issues across your organization
- All property conditions should be fully described (e.g., some consultants describe only the problem areas and do not note the conditions of all major property components/systems)
- All identified issues should have a recommendation and an associated cost
  - If the borrower provides cost information, the consultant must comment on its adequacy



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- Consultants should not repeat information
  - An executive summary should provide summary language for observations and recommendations; information from the narrative detail section should not be repeated verbatim
  - The conclusion/recommendation sections do not need to repeat the detail and analysis previously addressed
- Freddie Mac Forms 1103 and 1105 must be completed and certified by the consultant
- Reliance for report information must be provided to Freddie Mac as well as to the Seller