

## Common environmental due diligence mistakes to avoid

Under federal and many state laws, the owner or operator of a property can be liable for historical contamination at that property. That liability is strict – the property owner/operator need not have caused the contamination to be liable for an expensive cleanup. When acquiring property, or a business that owns/leases real property, the single best way to avoid environmental liability is to understand the environmental risk before buying the property or business. Knowing what you're buying allows you to manage, or avoid, the risk.

Environmental due diligence is therefore an essential element of any such transaction. In fact, the federal Superfund law includes two liability defenses for those who conduct thorough environmental due diligence: the innocent landowner defense and the bona fide prospective purchaser defense. Both are predicated on the purchaser (or new tenant) undertaking "all-appropriate-inquiry" into the environmental condition of the property. For most buyers, the all-appropriate inquiry standard means performing a Phase I Environmental Site Assessment under the standards set by ASTM International. The Phase I is designed to identify potential soil, surface water or groundwater contamination – called "recognized environmental conditions."

But merely having a Phase I in hand may not be enough. Some Phase I reports may have faulty conclusions or inadequate recommendations. Further, a Phase I may not identify all the potential sources of environmental liability. Proper environmental due diligence must include a carefully planned scope of work and a careful review of the Phase I report – relying on a flawed Phase I is not a defense to liability. To that end, we present five common issues we see when working with clients in the diligence processes.

■ **Failing to meet the current Phase I standard and its requirements.** A new ASTM Phase I standard (E1527-13) took effect in 2015.



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Compliance with the old standard no longer satisfies the "all-appropriate-inquiries" requirement of federal law. The new standard changed the Phase I in several critical ways. First, in addition to identifying RECs, the revised standard requires identifying "controlled recognized environmental condition" (CRECs) and "historical recognized environmental conditions" (HRECs). CRECs are environmental conditions that have been addressed to the satisfaction of a regulatory agency, yet hazardous substances remain on site, usually in soil or groundwater. CRECs often require future monitoring and maintenance obligations. HRECs reflect releases, which have been fully resolved with no remaining contamination or obligations.

Second, the new standard requires that vapor intrusion concerns be identified. Vapor intrusion involves the potential for chemicals in soil or groundwater to volatilize, enter buildings and create indoor air quality concerns. Vapor intrusion implicates potential statutory and common-law liability, including employee claims, toxic tort litigation and state-mandated remediation.

Finally, the new ASTM standard requires a more robust review of historical files related to the subject property. This enhanced file review can add significant time to the Phase I process.

■ **Failing to carefully review and negotiate the environmental consultant's contract.** Like any other contract, you should carefully review the terms and conditions



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that govern the relationship with your environmental consultant. Don't assume that the terms and conditions are reasonable. The most common problem we find is a consultant's attempts to limit its liability to either a low fixed amount or the amount paid for the Phase I. With environmental liability often reaching well into the hundreds of thousands of dollars and beyond, you should make sure that your consultant has some skin in the game when it comes to the risks associated with its Phase I reports. It's easy for a consultant to be careless if its risk is so low.

Likewise, consultant agreements should specifically spell out the consultant's insurance requirements across different policies, including professional, comprehensive general, employer and auto liability. Many other terms and conditions also can be critical to ensuring that the Phase I report provides the protection the buyer needs, including the scope of work, indemnity, who may rely on the report, confidentiality and reporting issues.

■ **Waiting until the last minute.** Thorough environmental due diligence takes time. Given the potential liabilities involved, careful consideration of environmental due diligence should be made at the outset of a transaction. Waiting until the week before closing is not a good plan.

■ **Relying on an old Phase I.** Phase I reports have a shelf life of only 180 days under the ASTM standard. While it may be tempting to save money and rely on an older report, such reliance would

not satisfy the all appropriate inquiry requirements under federal law. Instead, a buyer should obtain a new or updated Phase I to ensure that it obtains the benefits of the federal defenses.

Additionally, just like with a new Phase I, you need to be comfortable that the prior consultant, in the prior Phase I, did not miss any issues. The reality is that there are good Phase I's and there are bad Phase I's. If your current consultant relies on an older, flawed Phase I, your Phase I is equally flawed and the liability defenses may not be available. Consultants can make mistakes, and it is critical to identify and correct those mistakes to ensure that the Phase I you rely upon is accurate.

■ **Assuming that a Phase I is all the environmental due diligence you need.** There is no such thing as "one-size-fits-all" environmental due diligence. The appropriate level of due diligence depends upon the nature of the transaction itself. Is the subject property a turnkey office building or an old warehouse that will be redeveloped or torn down?

A Phase I is designed to identify potential soil, surface water or groundwater contamination at a property. It does not generally seek to identify asbestos-containing building materials or lead-based paint. Likewise, Phase I's do not assess compliance with environmental laws. If the target property or business has environmental permits, the Phase I may not identify the compliance status of those permits.

Potential environmental liabilities must be carefully managed in a real estate or business transaction. The first place to start is by knowing what the potential environmental liabilities are. This requires well-thought-out and reviewed environmental due diligence, which should minimally include an appropriate Phase I environmental site assessment.▲