



Buyer Beware:

New EPA Due Diligence Standards Will Impact All Commercial Real Estate Transactions

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Beginning November 1, 2006, every commercial real estate transaction will be subject to new federal regulations establishing environmental due diligence standards. Compliance with new regulation is a requirement for insulating buyers from potential liability under the federal Comprehensive Environmental Response, Compensation, and Liability Act ("CERCLA," also known as "Superfund"). CERCLA imposes liability, without regard to fault or negligence, on past and present owners for any environmental contamination found on the property, a purchaser of land contaminated by the activities of others is nonetheless liable under CERCLA unless it qualifies for one of few statutory defenses, such as those for bona fide prospective purchasers, innocent landowners, and contiguous property owners. However, to qualify for any of these defenses, a property owner must conduct "all appropriate inquiry" on or before the date of acquiring the property. Although conducting all appropriate inquiry is not the sole requirement to qualify for the CERCLA defenses, it is an essential first step. Despite the significance of the all-appropriate inquiry requirement, until recently, no federal statute or regulation defined that standard. As a result, prospective purchasers had



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little guidance on how to qualify for the CERCLA defenses. The new federal regulations confirm that a comprehensive environmental site assessment is a necessary part of pre-acquisition due diligence for every commercial real estate transaction.

THE NEW FEDERAL REGULATION MANDATES A PHASE 1 ENVIRONMENTAL SITE ASSESSMENT

The United States Environmental Protection Agency ("USEPA") conducted extensive negotiations

with interested parties to devise a comprehensive due diligence standard. The agency issued its final rule on November 1, 2005, entitled the "Standards and Practices for All Appropriate Inquiries." The rule effective on November 1, 2006, establishes federal guidelines for investigating the previous ownership and uses of a property for purposes of qualifying for any of the CERCLA defenses. Here are the key points that every real estate developer or investor should know about the new standard:

A PHASE 1 ENVIRONMENTAL SITE ASSESSMENT IS ESSENTIALLY MANDATORY

The new federal regulations require that real property purchasers conduct a comprehensive non-intrusive environmental site assessment, commonly known as a "Phase I." Although it has long been prudent practice to obtain a Phase 1 report, the new federal rules now make it mandatory to qualify for one of the CERCLA defenses. Compliance with the new due diligence standards is also a prerequisite to qualify for CERCLA grants for brown fields redevelopment

THE PHASE 1 MUST BE CONDUCTED BY A QUALIFIED ENVIRONMENTAL PROFESSIONAL

The all-appropriate inquiry investigation must be conducted

or supervised by an environmental professional. Before retaining an environmental consultant to perform a Phase 1 investigation, developers should ensure that the consultant is qualified under USEPA's definition of an "environmental professional" and is familiar with the new standards.

INCREASED SCOPE OF INVESTIGATION

The new federal rule generally requires a more comprehensive investigation than the old Phase 1 standards. An inquiry investigation must include interviews with past and present owners, operators, and occupants; reviews of historical sources of information: searches for recorded environmental cleanup liens; reviews of federal, state, tribal, and local government records; and visual inspections of the property and adjoining properties. In addition, the assessment takes into account any specialized knowledge the prospective purchaser may have about the property, any commonly known or reasonably ascertainable information about the property, and whether their purchase price of the subject property reasonably reflects the fair market value of the

property, if the property were not contaminated. Developers should expect the cost of Phase 1 investigations to increase as a result of the greater scope of inquiry.

EXPLICIT DOCUMENTATION

REQUIREMENTS APPLY

The new rule does not impose any new agency reporting or disclosure obligations. However, it does require that the environmental professionals conducting the inquiry satisfy certain documentation requirements intended to record their qualifications, their opinion as to whether the inquiry has identified conditions indicative of releases of hazardous substances at the property, and an identification of any data gaps in the information developed as part of the inquiry that may affect the conclusion.

PHASE 1 SITE ASSESSMENTS MUST COMPLY WITH THE NEW ASTM STANDARD E1527-05


A critical aspect of the final rule is USEPA's endorsement of ASTM International's revised Standard is widely accepted as the guidance document environmental consultants must adhere to in conducting a

Phase 1 environmental site assessment. A revised ASTM Standard was issued the same date as USEPA's promulgation of its final rule. USEPA's regulation endorses the 2005 ASTM Standard as "consistent with" the final federal rule and "compliant with the statutory criteria for all appropriate inquiries." The revised ASTM Standard is effective immediately, even though the final rule does not take effect until November 1, 2006.

Accordingly, developers should make sure that their environmental consultant complies with the 2005 revision of the ASTM Standard for any new Phase 1.

In addition to meeting the minimum standards set forth in the USEPA all-appropriate inquiry rule, the ASTM Standard is broader in scope than the federal rule. For instance petroleum products, which are excluded from CERCLA's definition of a hazardous substance, are included within the scope of the ASTM Standard. The ASTM Standard also contains more comprehensive inquiry and reporting requirements compared to the rule. Thus, a Phase 1 assessments that complies with the revised ASTM Standard not only satisfies CERCLA's all-appropriate inquiry requirement, but is an essential part of the pre-acquisition due diligence process.

CONCLUSION

USEPA's promulgation of the all-appropriate inquiry rule is a critical step to enable prospective purchasers to qualify for one of the CERCLA defenses. Compliance with the new federal rule will also provide developers with critical information about the environmental condition of a prospective purchase. Prudent developers should work with counsel and their environmental consultants to ensure that their pre-acquisition due diligence protocol satisfies the new federal requirements. 



General Differences	ASTM 1527-00	ASTM 1527-05	AAI
Environmental Professional (EP)			
Definition of EP	Generally defined, no specific licensing, education, or experience requirements	A person who possess sufficient specific education, training and experience necessary to exercise professional judgement to develop opinions and conclusions regarding conditions indicative of a release or threatened releases on, at, in or to a property-- Such a person must (i) hold a PE or PG license and 3 years experience; or (ii) licensed by the government, state, tribe or US territory to perform environmental inquiries and 3 years experience; or (iii) have a BS or higher degree in a discipline or engineering or science and 5 years experience; or (iv) ten years of experience	Same as 1527-05
EP Duties	Required to conduct site visits and interviews	"Responsible charge" of the project, must interview past owners, operators, and occupants, make declaration and opinion	"Responsible charge" of the project, must interview past owners, operators, and occupants, must address data gaps, make declaration and opinion
Historical Records			
Timeframe	"All obvious uses of the property shall be identified from the present, back to property's obvious first developed use, or back to 1940, whichever is earlier"	"All obvious uses of the property shall be identified from the present, back to the property's first developed use, or back to 1940, whichever is earlier"	From the present back to when the property first contained structures or was used for residential, agricultural, commercial, industrial or governmental purposes
Other historical sources	Any source or sources other than those designated... that are credible to a reasonable person and that identify past uses of the property. The term includes, but is not limited to miscellaneous maps, newspaper archives, and records in the files and/or personal knowledge of the property owner and/or occupants	Broadened to also include internet sites, community organizations, local libraries, historical societies, and current owners/occupants of neighboring properties	Same as 1527-05
Performance Factors	Reasonably ascertainable and likely to be useful	Publicly available, obtainable within reasonable time and cost restraints, and practically be reviewed; EP will make a reasonable effort to compensate for mistakes/insufficiencies in the information obtained	Same as 1527-05
Record of activity and use limitations and Environmental Liens	User's responsibility; the search results must be reported to the EP; and, scope of environmental cleanup lien search is limited to reasonably ascertainable land title records	No requirement as to who is responsible for the search; scope of environmental cleanup lien search includes those liens filed or recorded under federal, state, tribal or local law	Same as 1527-05
State and local officials	Requires reasonable attempt to interview local officials only	Federal, state, local and tribal records shall be checked	Same as 1527-05

General Differences	ASTM 1527-00	ASTM 1527-05	AAI
Interviews			
Current owner and occupant	A reasonable attempt must be made to interview key site manager and reasonable number of occupants	Mandatory	Same as 1527-05
Previous owners and occupants	No specific requirement; however, EP must ask questions during interview process regarding current and past uses of the property and adjoining properties	EP must interview past owners, operators, and occupants likely to have material information about the property if they have been identified and information is likely to be obtained and is not duplicative of information from other sources	Same as 1527-05
Nearby property owners	EP's discretion	In addition, interviews with at least one neighbor if the property is abandoned with evidence of uncontrolled access	Same as 1527-05
Government Records Review			
Delisted NPL sites	Not expressly required	1/2 mile radius	Same as 1527-05
CERCLIS/NFRAP Sites	Target/adjoining property only	1/2 mile radius	Same as 1527-05
IC/EC	User required to check land title records for AULs	Federal, state, and tribal IC/EC registries for property only	Same as 1527-05
Tribal Records	Not expressly required	Must be searched for Equivalent NPL, Equivalent CERCLIS, Landfill and/or solid waste disposal site lists, LUSTs, Registered storage tank lists, Voluntary cleanup sites, and Brownfield sites	Same as 1527-05
Site Reconnaissance			
Target Property	EP shall visually and physically observe the property	The property shall be visually and physically observed by a person with sufficient training and experience under the direction of the EP	Same as 1527-05
Adjoining Properties	To the extent that current uses of adjoining property are visually and/or physically observed	To the extent that current uses of adjoining properties are visually and/or physically observable	View surrounding parcels from one of the following vantage points: the property line, public right-of-way, or similar vantage point

General Differences	ASTM 1527-00	ASTM 1527-05	AAI
<i>Miscellaneous:</i>			
Shelf Life of a report/Updates	Updates of specific activities recommended after 180 days	Updates of specific activities recommended after 180 days	One year, with some updates required after 180 days
Reports	Present findings, opinions and conclusions	Specifically those data gaps that affect the ability of the EP to form opinions regarding environmental conditions	Same as 1527-05
Declaration	N/A	New declaration of experience and compliance with AAI regulation required by the EP	Same as 1527-05
Knowledge of User	The user must communicate any specialized knowledge or experience to the EP, and explain a reduced purchase price if it is significantly lower than comparable properties	The user must communicate any specialized knowledge to the EP, explain a reduced purchase price, communicate commonly known or reasonable ascertainable information about the property; and any obvious indications pointing to the presence or likely presence of contamination at the property	Not complete unless the assessment takes into account the relevant and applicable specialized knowledge and experience of user. Also, user must evaluate whether the purchase price is lower than fair market value as a result of contamination.
Objective of the ESA	To identify RECs	Same as 1527-00	To identify "conditions indicative of releases or threatened releases" of hazardous substances or petroleum products, if such releases would pose a threat to human health or the environment
Data Gaps	Report must document data failures and give reasons sources were excluded	No change to data failure language but adds new AAI requirement to document any data failure that significantly affects the ability to identify RECs, and meets new AAI requirements for documenting "data gaps"	Requires identification of sources consulted to address data gaps and comments on significance of data gap with regard to the ability of the environmental professional to identify conditions indicative of releases and threatened releases