



**ENVIRONMENTAL DUE DILIGENCE IN
COMMERCIAL REAL ESTATE TRANSACTIONS**



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Environmental Due Diligence in Commercial Real Estate Transactions

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Environmental Due Diligence in Commercial Real Estate Transactions

Why Do Environmental Due Diligence?

- Why Do It? How to Do It?
- Why Do I Need Another Lawyer in This Transaction?
- Why Can't I Just Order a Phase I Environmental Site Assessment Myself?



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Two Elements: Contract Drafting and Site Assessment

- Contract Drafting: allocates the liabilities and responsibilities consistent with the business deal
- You need proper reps, warranties, covenants & indemnities – forms won't do it
- Context is everything: what are the parties trying to accomplish?
- Site assessment: establish baseline property conditions, and plan how to remediate & otherwise deal with problems

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Contract of Sale: What Do You Need?

- DEFINITIONS: see Exhibit A
- Hazardous Materials: what to include
- Environmental Requirements
- Environmental Claims
- Adverse Environmental Condition

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Representations and Warranties

- What is a Representation?
- What is a Warranty
- These are No Substitute for Indemnity Provisions, or for Environmental Assessment

- Examples of Reps:
 1. Inducement/Best Knowledge
 2. Different Qualifiers
 3. No Violations/Compliance with Laws



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Representations and Warranties II

- All Required Permits (Permitted Properties) - Caveat: What's Not Covered
- "No Hazardous Substances/Hazardous Operations" – Issues:
 - *de minimis*, How Far Back, Seller's Own Use of Property
 - No Notices or Reasons to Expect One
 - No Asbestos, PCBs, USTs
 - Tricky Issues with Asbestos and PCBs

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“As Is” Clauses

- Need for specific language (see App. B) – no reps as to condition, restrictions, etc.; Buyer has inspected, opportunity to investigate, etc., waiver of objections or claims, assumption of risk vis a vis adverse P/P/F characteristics
- Seller should insist on Buyer release, but such release from contractual liabilities does not bar statutory claims
- Litigation Issues: first party v. third party claims
- Seller concession to buyer: don't release any other responsible party, and assign rights to sue



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Pre- Closing Covenants

- Typical are Promise (Covenant) by Party to Obtain No Further Action Letters, Close Inactive Tanks or do Remediation
- Maintenance of Representations: Seller to Keep Property in Compliance with all Environmental Laws and Reaffirm Representations and Warranties as of closing
- Environmental Site Assessments: Overview of Issues



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Indemnities

- Full & complete shifting of liability to another
- Stand alone is better; must be harmonious
- Pre-existing indemnities?
- Impact on statute of limitations
- Should cover presence, escape, etc., from property of Hazardous Materials; Environmental Claims arising under Environmental Requirements
- Any rep by seller being false/untrue materially

Indemnities

- Is there an obligation to defend?
- Indemnitor may want that obligation, in order to control costs
- Impermissibly broad indemnification is problematic
- Add “. . . to the fullest extent of the law.”
- Financial assurance mechanisms to back indemnity: escrows, bonds, letters of credit, insurance
- Other issues: extension to or from others, fixed time, fixed amount?

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Walk -Away Provisions

- Pre-closing ESA contingency (App. A): typically, if the ESA reveals an Adverse Environmental Condition – defined (Exh. A) as - presence of Hazardous Materials [Haz. Wastes or Hazardous Substances] on sale property or adjoining property (a) in violation of Environmental Requirements or in a condition which has caused or (b) such that it is reasonably likely to cause Environmental Claims, then either Seller must remediate, or Buyer may terminate (or variation thereof)
- Specify de minimis level of cleanup costs so Buyer cannot too easily walk away



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Existing Environmental Documents

- Seller must provide to Purchaser
- Helps seller organize what it has “knowledge” of, to ensure accurate representations re condition of property, e.g. that there is no contamination “except as described in the documents set forth in Appendix ___.”
- Improves the quality of the Phase I ESA, because consultant must review all available reports
- Saves time in preparation of the Phase I
- Minimizes any claims of undisclosed issues

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Post-Closing Cost-Sharing Provisions

- Advance Apportionment Good but not Easy
- Capping Amount of Seller's Exposure
- Deductible Amount – “Basket”
- Post-Closing Damages



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INSURANCE

- Cleanup Cost “Cap” Coverage: once considered helpful when sharing cleanup costs or where one pays but wants to control cost overruns, but no longer very available.
- Potential for revival of such coverage
- Pollution Legal Liability coverage: mainly third party bodily injury and property damage, with limited environmental cleanup coverage.
- Contractors pollution liability



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Site Assessments

- Why are They Necessary?
- Scope of Liability: Present/Past O/Os, Transporters, Arrangers
- Defenses: Acts of God, of War; Third-Party Defense (Denied to Person with Contractual Relationship, Except in Certain Cases)
- All Appropriate Inquiries into Prior Uses “Consistent with Good Commercial/Customary Practice”
- Owner/Operator Liability *Exemption* for *bona fide* Prospective Purchasers



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Phase I ESA

- ASTM “All Appropriate Inquiry” Standard
- Information Gathering (Requests for Documents, Historical Records, Title Searches, Database Searches)
- Site Visits by an Environmental Consultant
- Result: Identified “Recognized Environmental Conditions” (RECs)

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What is a “recognized environmental condition?”

- “the presence or likely presence of any hazardous substances or petroleum products on a property under conditions that indicate an existing release, a past release, or a material threat of a release of any hazardous substances or petroleum products into structures on the property or into the ground, ground water, or surface water of the property...”



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Phase II ESA

- “Invasive” (Soil, Groundwater Samples)
Investigation of RECs Based on Appropriate ASTM Standard
- Should be Performed After a Completed Phase I ESA (Even if Prior to Written Report)
- Determine Scope of Investigation Based on RECs

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Owner/operator liability exemption for bona fide prospective purchasers

- All disposal of haz sub occurred before acquisition
- “All appropriate inquiries” into previous o/ship and uses in accord with accepted good commercial and customary standards/practices
- Appropriate care with re HS found at property by taking reasonable steps to stop continuing release, prevent future release, & limit exposure to released HS
- Cooperation with response authorities & info requests
- Complies w land use restrictions/institutional controls
- Person not potentially liable/affiliated w contractual related to any other person who is potentially liable, exception contract acquiring property



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Compliance Audits

- In-Depth Examination of Facility Operations, Permits, Monitoring Records, Air Emissions, Discharges into Water, Waste Management, Right-to-Know
- Confidentiality Issues



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Environmental Consultants

- Choosing a Consultant
- Defining the Scope of Work
- Regular Contact, even Before Reports to Clients (Maintaining Confidentiality)
- Don't Rush the Process: Avoid Doing Phase II ESA if you Have Not Completed or Nearly Completed the Phase I ESA

Reporting Oil Spills To New York State

- Navigation Law
- Petroleum Bulk Storage Act
- “Any Person” Within 2 Hours
- Exception (Must Meet all Four)
 - Less than 5 Gallons
 - Under Control of Spiller
 - Will not Reach NYS Water or Land
 - Cleaned up within 2 Hours

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Reporting Oil Spills to the Feds

- Clean Water Act: Oil Causes a Sheen
- Owners of USTs: Oil Causes a Sheen or 25 Gallons
- CERCLA: Oil Exempted, but Must Report Release of a “Reportable Quantity” of any Hazardous Substance
- PCBs Under CERCLA and TSCA



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Conclusion

- Use Competent Environmental Professionals to Prevent Acquisition of Unnecessary Liability
- ***Good Contract Drafting + Good Environmental Site Assessments = A Deal that Reflects Actual Business Expectations and that Keeps the Government and Adjoining Property Owners Away***



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WHY DO AN ENVIRONMENTAL ASSESSMENT?

- Lender requires environmental assessment
- Owner/buyer wants to define environmental issues
- Required for Environmental Insurance application
- Owner/operator is required to do so under a Regulatory program
- To establish eligibility for an Innocent Landowner defense under CERCLA or an Innocent Purchaser defense under a State Spill or Brownfields Act
- Financial reporting obligations (SEC, FIN-47)

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ESTIMATING ENVIRONMENTAL LIABILITY AT PROPERTIES

- Soil Contamination
- Groundwater Contamination
- Asbestos
- Residual Hazardous Waste
- Vapor Intrusion from Off-Site



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ENVIRONMENTAL SITE ASSESSMENTS AND DUE DILIGENCE

- Discovering Soil and Groundwater Contamination
- Phase I Environmental Assessment
 - Recognized Environmental Conditions (RECs)
 - Historic RECs
 - De minimus RECs



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ENVIRONMENTAL SITE ASSESSMENTS AND DUE DILIGENCE

- Phase II Environmental Investigation
 - Installation and Sampling of Soil Borings
 - Geophysical Investigation
 - Monitoring Well Installations
 - Soil Gas Surveys

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ENVIRONMENTAL SITE ASSESSMENTS AND DUE DILIGENCE

- Contamination Discovery
 - Reporting Obligations
 - Source Confirmation
 - Delineation of Contaminated Media
 - Remedial Investigation (RI)



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SOIL & GROUNDWATER REMEDIATION CONSIDERATIONS

- Remedial Alternatives
- Hazardous/Non-Hazardous Determination
 - (aka: waste characterization)
- Source/Imminent Hazard Removal
- On-Site/Off-Site Issues

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POST REMEDIAL MONITORING & PROPERTY RESTRICTIONS

- Long Term Groundwater Monitoring
- Deed Notices
 - Institutional Controls
 - Engineering Controls
 - ❖ Caps (Concrete/Buildings/Landscaping)
 - ❖ Fences
- Biennial Inspections and Reporting



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REMEDIAL COST ESTIMATES

- Obtain Multiple Proposals
- Expect Large Ranges in Soil Volume
- Forecast Long Term Monitoring Requirements
 - Constantly Re-Evaluate Monitoring Plan
 - Design Monitoring Plan to Co-Exist with Land Use and Development of Property

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REMEDIAL COST ESTIMATES

- Include Site Restoration Estimates
 - Remedial Equipment Rental Agreements
 - Remedial Equipment Sell-Off
 - Monitoring Well Abandonment
 - Resurfacing
 - ❖ Pavement
 - ❖ Landscaping

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RELATED REGULATORY PROCESSES & COSTS

- Report/Oversight Fees
 - Review Timing Expectations
 - Response Letters



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RELATED REGULATORY PROCESSES & COSTS

- Wetlands and Stream Encroach Permits and Fees
- Source and Non-Source Discharge Permits (NPDES) and Fees
- Possible Natural Resource Damages

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REMEDIAL COST ALLOCATION

- Current v. Prior Owner Considerations
 - Joint and Several Liability
 - Multiple Source Delineation
 - Commingled Contamination
 - Historic Fill
 - Innocent Purchaser/Landowner



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REMEDIAL COST ALLOCATION

- On-Site v. Off-Site Source
 - Joint and Several Liability
 - Multiple Source Delineation
 - Commingled Contamination
 - Historic Fill



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ASBESTOS LIABILITY

- Asbestos Discovery Requirements
- Operations and Maintenance Programs
- Renovation & Demolition Abatement

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ASBESTOS DISCOVERY REQUIREMENTS

- Asbestos Surveys Required at All Buildings Constructed Before 1981
OSHA – 29 CFR 1926.1101(k)
- Survey Standard: ASTM E-2356-04
- Common Asbestos Containing Building Materials:
 - Floor Tile & Mastic
 - Roofing Materials
 - Thermal System Insulation (pipes, boilers, ducts)
 - Fire proofing, Acoustical Plaster

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ASBESTOS MAINTENANCE

- Asbestos can be managed in-place if an Operations & Maintenance (O&M)

Plan is prepared and O&M Program is implemented, including:

- Training Employees
- Providing Physicals and Medical Surveillance
- Labeling and Posting of Signs

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ASBESTOS ABATEMENT

- Renovation and Demolition Activities will typically trigger Abatement
 - Notify Multiple Agencies 14 Days prior
 - Obtain Bids from Licensed Contractors
 - Hire Independent 3rd Party Air Monitor
 - Perform Project Monitoring per ASTM E1368
 - Obtain and Retain copies of Waste Manifests, Air Clearance Samples, Project Monitor's Report (need to maintain for 30 years, per OSHA)

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RESIDUAL HAZARDOUS WASTES

- Ultimately all hazardous materials on site need to be characterized and properly disposed
 - Perform Inventory of Drums, Containers, Tanks, etc.
 - Maintain copies of MSDS Sheets & Characterize Wastes
 - Use Licensed Waste Haulers
 - Comply with Disposal Regulations (RCRA)
 - Maintain copies of Waste Manifests





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