

“NEW ENVIRONMENTAL DUE DILIGENCE STANDARD – EPA DECLARES WHAT DILIGENCE IS DUE”

Environmental due diligence is a prerequisite for identifying and managing environmental risks associated with any transaction involving real estate. For assets transactions, environmental due diligence also is a prerequisite to taking advantage of the three transaction-related defenses (innocent landowner, bona fide prospective purchaser, and contiguous landowner) under the Comprehensive Environmental Response, Compensation and Liability Act (“CERCLA”) or Superfund. Superfund is the federal statute that imposes strict and generally joint and several liability on, among others, owners and operators of contaminated properties, irrespective of whether they had anything to do with the contamination.

The New Rules

On November 1, 2005, the United States Environmental Protection Agency promulgated regulations prescribing the requirements for “all appropriate inquiries” (“AAI”), the level of due diligence required to take advantage of Superfund’s transaction-related defenses. Although sophisticated parties to real estate transactions will not hang their hat solely on AAI, conformance with it is one prerequisite to the Superfund defenses and, more importantly, AAI likely will set an industry-wide standard for minimum acceptable environmental due diligence.

The new rule includes requirements that: (1) the investigation be supervised by an environmental professional, a defined term; (2) specific interviews be conducted; (3) specific historical records be reviewed; (4) environmental liens and land use restrictions be searched; (5) local as well as state and federal records be reviewed; (6) visual inspections of adjacent as well as subject property be performed; and (7) data gaps be identified and evaluated. The rules also require that the investigation and various aspects of it be relatively fresh or updated. In addition, the rule places on the prospective purchaser responsibility for certain aspects of AAI, including, among other things, determining whether the purchaser price reflects fair market value for an uncontaminated property. The new standard goes

into effect on November 1, 2006. In the meantime, parties can use the new standard or the current standard, ASTM E1527-00. ASTM is promulgating a new standard, ASTM E1527-05, which EPA has indicated will satisfy the AAI requirements.

Some Caveats

First, to qualify for the transaction-related defenses, AAI is necessary but not necessarily adequate; parties must also satisfy prescribed continuing obligations, *e.g.*, implementing reasonable steps with respect to hazardous substances to stop and prevent releases and limit or prevent exposure. Second, the three defenses, even if available, do not protect against liability under other federal statutes, under state statutes, and under the common law. Third, AAI, as well as the current ASTM standard, does not address significant, non-CERCLA environmental concerns, *e.g.*, regulatory compliance, petroleum contamination, asbestos, lead based paint, lead in drinking water, wetlands, endangered species, and indoor air quality.

Some Observations

In light of this new rule, parties involved in transactions may wish to reexamine their current due diligence practices. As the caveats intimate, blindly following the rule may not always provide the protection a party seeks, or believes that it is receiving. Having a knowledgeable professional review present procedures and participate in the assessment loop is advisable.

For further information concerning these new rules and their effect on your business activities, please contact:

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