

# Don't Let Environmental Hazards Drag You Down

Assess a property's risk exposure pre-purchase to avoid costly post-transaction liabilities

By Michael Novak

**T**oday's real estate market is heavily influenced by environmental concerns. Anyone having a financial interest in real estate needs to know if potential environmental problems may involve them in expensive cleanup and lengthy litigation.

Extensive liabilities resulting from leaking underground storage tanks, buried industrial waste, poor-quality fill material, improper handling of hazardous materials, historic PCB usage and toxic spills have significantly changed the way business is conducted with regard to the ownership, management and transfer of property. It is essential for any real estate investor to assess and understand the associated risks and liabilities related to potential environmental contamination.

The burden is on lenders and property buyers to make a diligent effort to research and determine if any environmental hazards are associated with the property being acquired. Likewise, commercial mortgage brokers need to understand and be aware of any potential environmental risks linked to a property being eyed for purchase, in order to properly serve their clients.

## Hire an expert

To ensure a proper assessment of risks, prospective buyers of commercial property should consider retaining an environmental consultant immediately upon execution of the sales contract. Sellers, their brokers and other agents also should anticipate that any buyer will perform a thorough evaluation and may choose to address known issues in advance. Therefore, it's important to ensure that the due-diligence period provides sufficient time to perform a thorough assessment,

and allows for time extensions if recognized environmental conditions are discovered.

A key part of the review process is a Phase I Environmental Site Assessment, which is the first step in evaluating a property's environmental status and can help limit ultimate liability should the property be found to pose an environmental risk. Although there are currently no federally enforceable requirements for conducting a Phase I assessment, state requirements and industry guidelines recognized by the U.S. Environmental Protection Agency do exist — such as the ASTM (American Society for Testing and Materials) Standard E 1527-13.

There are numerous concerns that commercial mortgage brokers need to be aware of in order to assist clients in working effectively with an environmental consultant on a commercial or industrial property transaction. For starters, it is critical to determine if the environmental consultant routinely works in the state where the property is located and whether they maintain the licenses and certification required to address any problems that are discovered.

## Understand your exposure

When an environmental consultant submits a cost estimate for proposed remediation services, a mortgage broker representing a buyer in the transaction should make sure it is clear whether that buyer will inherit any post-closing, long-term monitoring obligations — and if the costs for those obligations need to be negotiated between the seller and buyer. Keep in mind that the seller may be able to complete post-closing remediation, utilizing an access and escrow agreement.

The broker also should establish whether the cost estimate for any required remedia-

tion is based on the collection and analysis of sufficient soil and groundwater samples, or on a broad estimate without the benefit of site data. In addition, the broker and client should determine if the estimate for remediation includes the following:

- **Post-case monitoring obligations** and maintenance mandated by an enforcement agency;
- **Costs related to restoring** concrete, landscaping and other cosmetics damaged by the remediation; and
- **Litigation costs expected** to be incurred by the responsible party related to neighbors that have been adversely impacted, or related to neighbors that are partially responsible for the contamination.

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### Assess future liabilities

When contamination is encountered, brokers will need to verify whether it is “discreet” and can be managed during a finite period, or if it is comingled with a neighbor’s problem — which would either extend the life of the cleanup, increase the cost or both. If the seller’s remediation involves contamination migrating off-site and under neighboring facilities, clarify whether or not the buyer may be exposed to potential litigation.

The buyer’s future plans for the property may raise additional concerns. If demolition is planned, the buyer may need to request that the consultant include an evaluation for asbestos-containing materials or other considerations that are beyond the scope of the Phase I Environmental Site Assessment. Other key considerations to address upfront include the following:

- **Whether the buyer’s plans** involve construction of a new building over a portion of the property that is still the subject of ongoing soil or groundwater investigations;
- **Whether or not the buyer’s future** use and occupancy can withstand a seller’s post-closing visits to the property to perform monitoring, investigations and possible remediation; and

- **Whether future development** at the property will be restricted in the event engineering controls must be employed to cap contamination.



It’s important for mortgage brokers to remember that commercial property buyers can establish protections under the law only if they ensure a Phase I Environment Site Assessment is conducted on the property, which can best be accomplished by hiring a qualified environmental consultant. That assessment also must comply with the ASTM standard as well as the requirements of the state or jurisdiction involved.

Unfortunately, there are too many instances in which commercial property buyers get hit with excessive remediation costs that were discoverable pre-purchase through a simple review of public information, such as historical aerial photos, fire-insurance maps and copies of environmental reports available from state agencies. Working with an experienced environmental consultant will arm a prospective property buyer with critical information and appropriate cost estimates for remediation, which can be negotiated to the satisfaction of all parties — without jeopardizing the deal. ■