

Environmental Due Diligence Beyond the Phase I

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Many attorneys advise clients to have a Phase I Environmental Site Assessment (ESA) done when purchasing real property. However, Phase I ESAs are limited in scope and only identify indications of contamination within the property. For transactions involving existing businesses and facilities, a Phase I ESA does not tell the buyer anything about whether the facility is operating in compliance with the various environmental laws and regulations that may apply to its activities. In addition, when planning a new development or expanding existing facilities, the buyer must understand any applicable environmental regulations that may restrict such plans. Again, this issue lands well outside the scope of a Phase I ESA.

This article identifies some of the regulations that may govern an existing business's operations, discusses how to identify such compliance issues in a business transaction, and provides some examples of factors that can limit a new or expanded facility's location.

Getting an ESA before you buy

Buyers should consider getting a Phase I ESA before purchasing real property for a couple of reasons. On a practical level, the ESA provides information to the buyer regarding indications of contamination within the property. And, as a legal matter, conducting a Phase I ESA or "all appropriate inquiry"¹ satisfies one of the requirements for the "bona fide prospective purchaser" defense and other liability defenses.² Without

What properties need an ESA?

Generally speaking, this article applies to transactions involving non-residential (agricultural, industrial, commercial, etc.) properties, as well as multi-unit residential properties. As EPA has recognized, typical activities on small residential properties do not generate contamination. Therefore, conducting a Phase I ESA in the context of a single unit residential property transaction is usually unnecessary, and

is relatively rare. However, the statutes governing liability for contamination (which will be discussed in more detail later in this article) do not categorically exclude residential properties (and the owners thereof) from liability. Instead, EPA and many state agencies have policies of not enforcing against owners of contaminated residential properties who did not otherwise contribute to the contamination.

such defenses, the owner of a contaminated property could be one of the parties liable for such contamination.³

A Phase I ESA must be conducted by a qualified environmental professional and includes a site visit, review of environmental databases and historical records, interviews with past and present owners and occupants, interviews with state or local government representatives, and, finally a written report about the investigation and whether there are any "recognized environmental conditions" on the property that warrant further investigation.⁴ The Phase I ESA includes potential contamination by a wide variety of "hazardous substances" and petroleum products. Interestingly, even though one of the primary reasons to conduct the assessment is to qualify for liability defenses as previously described, petroleum product contamination is not subject to all of the same rules and defenses as other pollution. However, the standard Phase I ESA includes petroleum contamination because, historically, it has been a concern at many properties.⁵

Even though Phase I ESAs deal with a wide variety of "hazardous substances" and petroleum products,

many other issues and concerns may warrant assessment that are not commonly included in a Phase I ESA. These "non-scope" issues include asbestos, biologic agents, cultural and historic resources, lead-based paint, radon, threatened or endangered species, and wetlands.⁶ If any of these issues are of concern, they must be separately assessed or specifically added to the scope of the Phase I.

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Recent updates clarify the ESA scope

Before discussing some of the compliance and other “non-scope” issues, it may be helpful to briefly note some recent revisions to the standards governing Phase I ESAs. In November 2013, the Phase I ESA standard protocol was revised by its sponsoring organization, ASTM⁷ International. Some of the changes should help property owners avoid stigma from past problems that have already been resolved. The changes include:

- The definition of a “recognized environmental condition,” which could trigger the need for additional investigation with a Phase II ESA.⁸ While the prior definition was cumbersome and potentially confusing, the revision looks squarely at “releases” that could lead to cleanup liability under federal law.
- Differentiating between past releases that have been remedied, past releases that are being controlled by treatment or site restrictions, and current contamination.⁹
- Clarification that de minimis conditions that do not pose threats to human health or the environment are neither “recognized environmental conditions” nor “controlled recognized environmental conditions” that require further investigation.¹⁰ (An example might be a small spill on pavement that has been cleaned up.)
- Making the potential presence of vapors from contaminated soil migrating into living and work areas, or onto other properties, a standard component in Phase I ESAs.¹¹

In addition to these revised standards governing Phase I ESAs, new database research products are constantly evolving. Depending on the level of sophistication needed,

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these tools can reduce the costs of researching regulatory files and historical records. However, they are not a replacement for the professional interpretation required by the ASTM Phase I standard.

Compliance issues

While the information generated in a Phase I ESA is very important, it is also quite narrow in scope. In the case of an existing facility, the Phase I ESA does not examine compliance with the myriad environmental laws and regulations.¹² And, in situations where a purchaser may want to construct a new facility or expand an existing one, the Phase I ESA does not identify potential environmental regulatory hurdles or limitations that could restrict those plans.

Environmental audits generally

Because environmental compliance issues may arise, the buyer should consider an environmental audit in addition to the Phase I ESA. Increasingly, large companies demand their vendors and suppliers implement environmental auditing programs as a threshold requirement. Therefore, environmental audits have utility even outside the transactional context.

Some of the most common areas of environmental regulation include

the emission of air pollutants under the Clean Air Act,¹³ the discharge of wastewaters to surface waters under the Clean Water Act,¹⁴ and the management of hazardous waste under the Resource Conservation and Recovery Act.¹⁵ Some programs also apply to drinking water quality; managing used oil; storing and managing petroleum products, fertilizers, pesticides and other chemicals; construction activities on structures with asbestos and lead paint; managing refrigerants containing chlorofluorocarbons (CFCs); and others.

With an environmental audit, an environmental consultant evaluates whether the facility is in compliance with these various programs. In addition, the environmental audit can evaluate the regulatory climate and, in particular, whether there are any known issues that may limit construction of a new facility or expanding an existing facility. The remainder of this article explores examples of additional environmental considerations for a commercial or industrial property buyer.

Ambient air quality standards can affect new and expanding facilities

Under the federal Clean Air Act, the Environmental Protection Agency (EPA) establishes ambient air quality standards for six pollutants

referred to as “criteria” pollutants: carbon monoxide, lead, nitrogen oxides, ozone, particulate matter, and sulfur dioxide.¹⁶

To measure these, each state, including Idaho, is divided into several airsheds. The state tests the ambient air at various monitoring stations, and EPA criteria for the frequency of exceedances within a two or three-year period determine whether each airshed is in compliance with the ambient standards. Areas that remain in compliance with the ambient standards earn designation as “attainment” areas, and areas with criteria pollutants consistently exceeding the ambient standards are designated as “non-attainment” areas.¹⁷ The distinction between “attainment” and “non-attainment” areas is important because different permitting standards and requirements apply to each.

A facility that will emit any of these criteria pollutants above EPA thresholds must obtain an air permit from the Idaho Department of Environmental Quality (DEQ) before construction or modification of the facility begins.¹⁸ To receive the permit, a facility located in an “attainment” area must demonstrate to DEQ that it will not cause or significantly contribute to violations of the federal ambient standards or state toxic emission standards, and that its air emissions will comply with the technology-based “best available control technology” emissions limitations.¹⁹

By contrast, a facility located in an area that has already been designated as non-attainment must utilize even stricter technology-based emissions standards that achieve the “lowest achievable emission rate.” The facility must demonstrate that it will not significantly contribute to

ambient concentrations of the non-attainment pollutant which, in some cases, requires the facility to “offset” its emissions of the non-attainment pollutants by securing reductions in emissions by other sources within the airshed.²⁰ Therefore, when deciding whether to construct or expand a facility, it is important to consider the airshed’s compliance with ambient air quality standards.

Here in Idaho, non-attainment areas include the Cache Valley in the southeastern corner of the state for fine particulate matter (PM_{2.5}, which is commonly attributable to emissions from motor vehicles, combustion, heating appliances, etc.), and the Pinehurst area of the Silver Valley, both for fine particulate matter (PM_{2.5}) and for coarse particulate matter (PM₁₀, commonly generated by road dust and agriculture).²¹

In addition to existing non-attainment areas, some airsheds are considered areas of concern and are therefore potential candidates for future non-attainment designations because there have been a significant number of measurements exceeding the ambient standards. One such area is the Ada and Canyon County Area for both fine particulate matter (PM_{2.5}) and ozone (O₃).²² The key source of ozone in the Ada and Canyon County Area are nitrogen oxides (NO_x) from motor vehicles combin-

ing with volatile organic compounds (VOCs)²³ typically derived from fuels, paints and coatings, and some process chemicals. Air emissions modeling has shown that reducing VOC emissions will be key to reducing ozone in the Treasure Valley — a potential indicator of future regulatory attention.²⁴

To summarize, a new or expanded facility in a non-attainment area will face much more stringent permitting requirements than one located in an attainment area. Put another way, locating or expanding a facility in a non-attainment area can be significantly more expensive due to the additional pollution controls that would be required. Businesses currently located, or that wish to locate, in these areas should consider these issues early in the planning process. A traditional Phase I ESA would not alert a buyer to such issues.

Locating a facility near impaired surface waters

Many operations and facilities generate waste waters that must be discarded, such as food processing facilities, power plants, and municipal treatment plants. In addition, construction sites and certain industrial facilities discharge storm water runoff to nearby creeks, streams, and rivers. Under the federal Clean Wa-

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ter Act (CWA), in order to discharge those waste waters to a nearby surface water body, the facility must first obtain a discharge permit from EPA.²⁵

The CWA also requires all states, including Idaho, to designate the types of uses that each surface water body should be able to support.²⁶ An “impaired” water body is one that does not meet the water quality criteria necessary to support the designated uses. When this occurs, a “total maximum daily load” (TMDL) is then developed for that pollutant within the impaired water body.²⁷ Essentially, a TMDL is the maximum amount of the pollutant that the water body can contain and still meet the applicable water quality standards.²⁸ These TMDLs are then used to set the effluent limitations, monitoring requirements, and other conditions in the individual permits that authorize discharges into that water body.²⁹

Water body assessments and, in some cases, TMDLs, have been completed for 67 water quality sub-basins in Idaho. As of 2012, 36% of streams and 56% of lakes are not fully supporting state water quality standards, with 34% of streams and 38% of lakes having not yet been assessed at that time.³⁰ In Idaho, TMDLs have been developed and approved by EPA that cover nearly 24,000 miles of rivers and streams and over 210,000 acres of lakes and reservoirs.³¹ This is important information to know for facilities located or proposed in these areas, because it can be expensive to achieve the pollution reductions in a wastewater stream necessary to comply with the TMDL-based effluent limits. Again, this type of information is well outside the scope of a typical Phase I ESA.

Locating a facility in problem areas for groundwater

The federal Safe Drinking Water Act (SDWA) regulates the quality of drinking water provided by municipalities, subdivisions, and commercial establishments whose drinking water is not provided by a municipality or other utility supplier.³² In Idaho, DEQ administers the SDWA. Its regulations apply to any business or establishment that regularly provides drinking water to an average of at least 25 people daily for at least

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60 days out of the year, and to any system with at least 15 service connections.³³ Among other responsibilities under the SDWA, regulated facilities must sample and treat their water to ensure pollutants fall below certain thresholds.³⁴

Nitrate is one of the most widespread ground water contaminants in Idaho, a state where ground water supplies 95% of the drinking and industrial supply. Of 34 nitrate priority areas in Idaho, many already exceed or are close to exceeding the SDWA standards. Because mu-

nicipalities and businesses cannot provide water exceeding the SDWA drinking water standards, contaminants in local groundwater can limit operations or expansion, or require a facility to implement expensive water treatment techniques. Again, this important information falls outside the scope of a typical Phase I ESA.

Conclusion

Phase I ESAs provide real property buyers with key information regarding potential contamination. They are also essential for certain liability defenses. However, ESAs are fairly limited in scope. Depending on the transaction, it may be prudent to expand the due diligence to include assessing compliance with environmental permits and requirements, and whether such requirements may hinder plans for future development or expansion. This article has identified some of the issues that warrant a complete environmental picture of a particular property or facility.

Endnotes

1. The contents of a Phase I ESA are governed by industry standards promulgated by ASTM International, while the contents of an “all appropriate inquiry” are governed by EPA regulations. *Compare* STANDARD PRACTICE FOR ENVIRONMENTAL SITE ASSESSMENTS: PHASE I ENVIRONMENTAL SITE ASSESSMENT PROCESS E1527-13 (ASTM International 2013) (hereinafter, “ASTM Standard”), with 40 C.F.R. Part 312 (EPA “all appropriate inquiries” rules). Unless otherwise noted, references in this article to Phase I ESAs should be read to also include an “all appropriate inquiry” investigation pursuant to EPA standards, and vice versa. By way of background, ASTM’s revision of the Phase I ESA standard preceded EPA’s revision of its “all appropriate inquiries” standard, but the federal agency caught up a month later. EPA’s revised “all appropriate inquiries” standard clarifies that the ASTM E1527-

13 standard is compliant with the EPA rule, and that parties conducting all appropriate inquiries may use the procedures in the ASTM E1527-13 standard. 40 C.F.R. § 312.11(c).

2. 42 U.S.C. § 9601(40).

3. 42 U.S.C. § 9607(a)(1).

4. See ASTM Standard, note 1, §§ 1.1.1, 7.1, 7.3.1; 40 C.F.R. § 312.20(e).

5. *Id.*, note 1, § 1.1.2.

6. See *id.*, note 1, § 13.

7. Until 2001, this organization was known as the American Society for Testing and Materials.

8. See *id.*, note 1, § 3.2.78.

9. See *id.*, note 1, §§ 3.2.18, 3.2.42.

10. See *id.*, note 1, §§ 3.2.18, 3.2.22, 3.2.78.

11.

12. See *id.*, note 1, § 3.2.30.

13. 42 U.S.C. §§ 7401-7671q.

14. 33 U.S.C. §§ 1251-1387.

15. 42 U.S.C. §§ 6901-6992k.

16. See 40 C.F.R. Part 50.

17. See generally 42 U.S.C. § 7410.

18. IDAPA 58.01.01.201.

19. 42 U.S.C. § 7475(a); 40 C.F.R. § 52.21(j); IDAPA 58.01.01.205.

20. See 42 U.S.C. § 7503(a); IDAPA 58.01.01.204.

21. See generally IDAHO DEPARTMENT OF ENVIRONMENTAL QUALITY, ATTAINMENT VERSUS NONATTAINMENT, at <http://www.deq.idaho.gov/air-quality/monitoring/attainment-versus-nonattainment.aspx> (last visited March 9, 2015).

22. *Id.*

23. DIVISION OF ATMOSPHERIC SCIENCES, DESERT RESEARCH INSTITUTE, OZONE AND ITS PRECURSORS IN THE TREASURE VALLEY, IDAHO 20, 22 (2008).

24. See generally *id.* at 136.

25. 33 U.S.C. §§ 1311, 1342; 40 C.F.R. § 122.21. As a result of legislation passed in 2014, Idaho is currently putting together an application package to obtain authority from EPA to administer this permitting program. See IDAHO CODE § 39-175C.

26. 40 C.F.R. § 131.10.

27. 33 U.S.C. § 1313(d); IDAPA 58.01.02.055.02.

28. IDAPA 58.01.02.010.100; 40 C.F.R. § 130.2(i).

29. 33 U.S.C. §§ 1311(b)(1)(C), (m)(2), 1342(a)(1)(A); 40 C.F.R. § 130.7(a).

30. IDAHO DEPARTMENT OF ENVIRONMENTAL QUALITY, IDAHO'S 2012 INTEGRATED REPORT xii (2014).

31. *Id.* at xi.

32. See generally 42 U.S.C. §§ 300f – 300j-26.

33. See IDAPA 58.01.08.003.107.

34. See generally IDAPA 58.01.08.

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