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NAVIGATING THE MUDDY WATERS OF ENVIRONMENTAL INVESTIGATIONS IN LAND USE

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I. OVERVIEW

A. The Perspective of This Paper

The idea for this paper originated in the practical experiences of the authors. Over their careers we have both seen certain common mistakes made by buyers and sellers of real estate in how they perform environmental due diligence investigations. These common mistakes run the gamut from failing to realize a particular Property requires certain investigations, to failing to appreciate the time requirements to overcome regulatory obstacles presented by some projects.

We also see clients unfamiliar with, confused by, and frankly scared of, environmental due diligence. So we set out to write a paper to assist developers, and their attorneys and consultants, to better understand the plethora of environmental investigations that may be required in developing Properties, and to more quickly identify the ones applicable to any particular property.

This paper is not limited to private developers. Some may find it interesting, karma perhaps, that governments can be subject to more environmental regulations than private developers, when governments disturb land for purposes of development. As such, practitioners counseling governmental entities may also find this paper relevant to their clients.

There are two authors with different expertise. We originally considered identifying which of us made suggestions and opinions, which would have awkwardly required us to refer to ourselves in the third person. But as we worked together we found that our views were comfortably similar. Our war stories of projects gone wrong had common causes. So we revised the paper and frankly it now better reflects the teamwork approach that best addresses environmental due diligence.

B. The Timberline

This paper generally addresses environmental investigation issues as they normally appear chronologically in an ideal (from the perspective of us environmental lawyers and consultants) purchase and development scenario, which looks like this in condensed form:

1. Enter into an Access Agreement and Confidentiality Agreement regarding the Property and information about the Property
2. Conduct a Phase I ESA of the Property within 180 days prior to acquisition
3. Conduct a Phase II ESA of the Property
4. Enter into an Agreement of Purchase and Sale for the Property
5. Purchase the Property
6. Conduct a jurisdictional determination of Waters of the United States on the Property
7. Conduct a Threatened and Endangered Species Investigation on the Property
8. Conduct a Cultural Resource Assessment of the Property
9. Complete a Site Design for the Property

It is not unusual for the parties to enter into an access agreement and confidentiality agreement after signing the Agreement of Purchase and Sale, or to include these terms in the Agreement of Purchase and Sale. The only issue that may create is the need to amend the contract if investigations require additional time to complete. After signing a contract, sellers often want to be compensated for that extra time and increased access. The nine steps listed above are intended to help avoid these sorts of negotiations but we fully recognize these nine steps are the most conservative process and may not fit every situation.

Unfortunately, not all developers follow this Timberline. The authors have been involved in projects where the prospective purchaser starts with draft site designs. Practically, some developers use a site design to help determine how much they are willing to pay for a Property. This paper will not address site design issues. The purpose of the environmental due diligence described herein is to allow the buyer to eventually

complete a site design for the Property that takes into account all areas of the Property that cannot be developed or will have some sort of restriction affecting development.

C. No Air Quality Issues

This paper is limited to environmental issues affecting the surface and subsurface of real property. As such, it does not address air quality issues or airborne contamination, unless the air quality issue is a recognized environmental condition (REC) identified in a Phase I Environmental Site Assessment (ESA).

D. "AS IS" Purchase

Unless the context clearly indicates otherwise, this paper assumes the seller desires to sell the Property"as is", meaning the seller will not make any representations or warranties that may affect the due diligence a prospective buyer should complete. One important note on "as is" transactions: an "as is" sale requires three different contract terms to actually be an "as is" sale under Texas law. One, it must convey the Property "as is" and disclaim all warranties. Two, the buyer must release the seller from liability for any and all environmental conditions of the Property. Three, each party must acknowledge that they have been represented by legal counsel and fully understand every term and condition in the contract.[1]

II. FIRST THINGS FIRST: ACCESS, REPORTING AND CONFIDENTIALITY

A. Access

The first issue for negotiation, sometimes (and certainly ideally) even before completion of a contract of sale and purchase, is for access to land to perform due diligence activities. Two of the most common issues regarding initial access and due diligence are:

1. Invasive testing; and
2. Whether the buyer will provide completed reports to the landowner/seller.

Invasive testing by a prospective buyer without prior seller/landowner approval is a trespass triggering liability to the landowner by the individual(s) and/or business conducting the testing, and by the prospective purchaser as their principal. Phase I ESAs do not require invasive activities. Phase II ESAs and Cultural Resources Assessments often do require invasive testing. Attached as **Exhibit A** is a form of Access Agreement generally favorable to the prospective purchaser that allows invasive activities. Attached as **Exhibit B** is a typical provision in a purchase and sale agreement which grants access to the land as part of an "inspection period" for non-invasive testing.

Few typical purchase and sale agreements allow for invasive testing. Invasive testing most often requires a separate access agreement, usually negotiated after execution of the purchase and sale agreement, and after a Phase I ESA shows the necessity for some sort of invasive testing. These negotiations also typically require the extension of inspection periods beyond the time the prospective buyer completes the additional due diligence.

Some practitioners routinely advise their clients to simply terminate the purchase contract if a Phase I ESA identifies an REC. In their view, RECs so fundamentally change the real estate asset that the buyer should renegotiate the entire contract, or at least some or all of the following terms:

1. Purchase price
2. Extra time to inspect the Property for additional due diligence
3. Allocating the cost of the additional due diligence between the seller and prospective buyer

[1]These three elements are derived from Texas case law and are now generally accepted by real estate practitioners. *See*, e.g., Baucum and Allen, *Protecting the Lender on the Sale of REO*, UTCLE Mortgage Lending Institute (2012), and the many prior CLE and other professional papers referenced on the "Credits" page therein.

Title search: Navigating the Muddied Waters of Environmental Investigations in Land Use

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