

Legal liability can hit property owners, tenants and even managers

by Diane Smith

Liability usually arises when someone has been negligent and, as a result of the negligence, another person has been damaged. When it comes to environmental damages, however, usual thinking about liability must be discarded.

Most environmental laws impose strict liability; that is, liability without regard to fault. This strict liability aspect of environmental law exposes both landlords and tenants to significant risks.

All those who own and control contaminated property, plus all those who owned or controlled the property when or after it became contaminated — all current and former owners and operators — are jointly liable. Tenants can be operators.

Since leases allocate liability by contract, responsibility provisions of environmental laws ignore contracts and leave the details of remedying conditions and paying damages to those jointly liable. The powers of regulatory agencies and the rights of third parties are not affected by lease terms.

Damages and liability

Often the question is how much each party should pay, and where the money will come from. Damages can include cleanup and compliance expenses; and liability for claims brought due to exposures to hazardous substances, bodily injuries, property damage, loss of income and diminished value. Soil and groundwater cleanups may be required. Liability can be breathtaking. Landlords and tenants, therefore, have big stakes in accounting for and managing environmental conditions and risks.

Leases are the customary means of al-

locating responsibility and deserve close attention, but they are not the end of the story in environmental matters. Protections in leases are only as good as the financial condition of the liable party. Leases may even make things worse. For instance, a lease may provide that the lessee assumes full financial and legal responsibility for the condition of the property, even if it has been contaminated by the owner, prior lessees or third parties.

Tenant and statutory rights

In such a case, the tenant may have given up statutory rights to demand that the landlord or others contribute to the cost of a cleanup, despite the fact that those others are clearly liable under the environmental laws. While a lease may impose liability on one party only, regulators usually will impose responsibility jointly, and leave the parties to work out the details. Leases must be drafted clearly and effectively, since courts scrutinize environmental terms closely, and construe such provisions as indemnities against the party who seeks to be protected.

However, actions speak louder than words in leases, where environmental-risk avoidance is the goal. "Environmental due diligence," assurance of adequate property management, and periodic reviews of current site activities and conditions ("tenant audits") can help significantly.

Document property condition

Environmental due diligence is the organized gathering and interpreting of information regarding a property. All parties should establish and document the condition of the property when the lease begins and ends. Specific attention should be directed to site history and use (particularly chemical use), regulatory records, existing conditions, prior conditions, changes to the property and on-site structures over time (such as tank removals and prior demolitions), nearby

and adjacent property uses, previous spills or incidents such as fires, and adjacent, nearby or regional concerns.

Review of regulatory records and permits, should be conducted. Anticipated property changes that could be impacted by subsurface conditions or materials such as asbestos or removal of PCB-containing light ballasts deserve special consideration. The presence of substances that may trigger requirements for notices, signs or special precautions should be noted.

Landlords should evaluate tenants from financial capability and environmental-awareness standpoints and assure that the tenant properly manages the property. Owners should understand activities to be conducted on the property, approve the quantity and identity of substances to be used, assure that lessees' plans and procedures for managing chemicals, wastes and potentially polluting processes are adequate, control all necessary modifications to the property and conduct periodic tenant audits.

Shocking property managers

Property managers can greatly assist owners in liability management. In fact, property managers may be shocked to find that they are considered operators if they have day-to-day operation and control of real estate. While tenants' rights to occupy, operate and control property give tenants the best ability to prevent environmental harm, landlords are well advised to assure that appropriate measures are undertaken.

Though many a landlord's contact with the lessee is the monthly rental check, only those who enjoy high-risk activities should rely on tenants to manage and protect property from an environmental standpoint. Tenant audits, which are periodic reviews of property operation and conditions, are invaluable from a liability-control standpoint. Audits should be conducted carefully to assure confidentiality, allow prioritization and avoid unex-

pected consequences in the audit findings.

Here is a checklist of steps which can be taken to avoid environmental liability in lease transactions:

- Perform adequate environmental due diligence before leasing and upon lease termination.

- Investigate tenants' environmental-compliance records.

- Assure financial capability (security deposits, parent guarantees, etc.). Increase such security if circumstances warrant.

- Negotiate effective lease provisions: warranties, representations, indemnities, releases, insurance, premises description, ownership/use of facilities and fixtures, and removal of equipment such as underground tanks must be drafted with environmental laws in mind.

- Monitor and establish compliance through periodic audits.

- Enumerate protective measures in the lease and require evidence of compliance.

- Draft the lease to permit either party to undertake additional investigations or actions.

- Address the parties' obligations to report hazardous substance releases and provide notices and warnings.

- Require each party to keep the other fully informed as to regulatory actions, claims or conditions that could lead to liability.

- Prohibit changes in site use without prior approval.

- Address rights to vacate the premises if environmental problems are later discovered, even on adjacent or nearby prop-

erties.

- Specifically address liability for known conditions of concern, allocate responsibility and schedule action.

- Address responsibility for disposal of contaminated soil and other wastes if cleanups are ever performed.

- Make regulatory issues such as waste disposal, hazardous-materials management and permit compliance noncurable events of default.

- Prohibit all but essential chemicals, and allow those only in reasonable quantities and controlled circumstances.

- Tightly control and supervise all renovations that could involve asbestos disturbance or disposal of hazardous substances such as PCB-containing light ballasts.

- Maintain copies of all permits, waste-shipping documents, hazardous-materials management plans, and other regulatory records. Assure that agencies provide copies of all notices of violations, correspondence, etc.

- Address reimbursement for civil penalties or other environmental costs and expenses.

Environmental laws and regulations change frequently and show no signs of becoming less stringent. For example, a new state statute imposes reporting obligations and penalties for noncompliance on owners of property even if they have not caused the release. Under this new law, and many others, what you don't know can cost you \$25,000 a day. When dealing with real estate, environmental issues must be a central focus — the consequences of a problem are too significant to overlook.