

FROM CONTAMINATED PROPERTY TO PRODUCTIVE USE

Liability issues for building owners, tenants

By DIANE R. SMITH

According to most airline pilots, aircraft engaged in lengthy flights are frequently, if not almost constantly, off course. Constant course adjustments must be made to assure that the desired destination will be reached.

This startling statement could also describe our environmental regulatory system. We have been slightly off course, and corrections are under way.

Facilitating the return of "environmentally challenged" properties to productive use is just one such course correction. And it is a correction that benefits everyone, including property owners and the general public. And, most notably, it is being accomplished without repeal of our environmental laws.

Environmental issues haunt any real estate transaction involving contaminated property. Overcoming obstacles and making a transaction work well for the parties is one of the most rewarding activities in environmental law today.

Pervasive issues

With respect to prospective buyers or tenants, both perceived and actual potential liability for cleanup or response to enforcement actions by regulatory agencies must always be addressed. Employee concerns regarding potential exposures and the possibility of additional workers' compensation or third-party "toxic tort" claims pose additional issues, as do the possibilities of business interruption or site disruption due to remediation activities.

Tenants or potential purchasers may be apprehensive about when and how certain on-site activities are conducted, including those requiring personal protective equipment for workers. Will required remediation interfere with the intended use or result in adverse public relations? Potential buyers may be wary of the possible impact of inducing a "stigma" on value, future sales or financing. The scope of indemnities to buyers and potential tenants is always a subject for negotiation.

Sellers and landlords

Similarly, sellers and landlords focus on the transaction's effect on their business interests. Will they have continuing and future remediation, enforcement or toxic-tort exposure after the sale or lease? What responsibility will the purchaser or tenant assume? How will the purchaser or tenant performance be assured? And what future site impacts by purchasers or tenants may affect the landlord's or the owner's liability, or make remediation more difficult or expensive? Who will have control over remediation methods and timing, and what cleanup standards will be utilized? What requirements does the buyer or prospective tenant have with respect to indemnity?

It's possible to address all concerns of buyers, sellers and tenants and to get deals done. Addressing all of the concerns is not only possible, it's happening.

Innovative programs

There are new, useful approaches, programs and policies at both the state and

federal level that have proven to be of real assistance in recent transactions, and which hold great promise as tools for making contaminated property less of a problem and more of an asset.

Many very useful initiatives exist at the state level, which, in many instances, prove to be of more value than the federal programs, which are of less sweeping applicability.

The California Expedited Remedial Action legislation, passed in 1994, is a good example of a new program that offers substantial benefits to purchasers and sellers in both cost savings and liability protection.

This recently implemented legislation is

designed to coordinate agency requirements, speed remediation, provide a site-specific cleanup focus and expedite projects. It does all this while providing significant incentives in liability protection for responsible parties, as well as for future purchasers of contaminated real estate.

The state's Water Resources Control Board's proposed Non-Attainment Zone Policy should improve the logical and technical underpinnings of groundwater cleanups and reduce expenses. It will allow "non-attainment" of certain water quality standards where "attainment" is not reasonable, feasible or sensible.

Recent policy statements have been issued

by the Board with respect to the necessity and nature of cleaning up contamination from leaking underground petroleum storage tanks. Such statements can only help reduce the cost of managing some sites, as no cleanup, but only monitoring, will be required. Though both the non-attainment and petroleum site policies are very new, they will probably affect a number of matters favorably. Combined with the state's new attitude toward the necessity and extent of groundwater cleanups, the policies may have great effect.

At the federal level, the Environmental Protection Agency's revised model consent agreement addresses some of the criticism

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made by users of the former model agreement.

The revised model agreement should make settlements less controversial and tedious to negotiate, therefore making it easier and less costly to achieve. This should expedite cleanups and resolution of site conditions.

Cleanup levels will vary with the expected future uses of property as a result of the EPA's recent directive on future land use considerations. "Comfort" letters, indicating the EPA's decision not to pursue certain parties with respect to an environmental issue, as well as prospective purchaser agreements resolving liability for buyers of contaminated property, will provide additional layers of "comfort" to parties involved in sites transactions.

Expedited settlements with current landowners who have not contributed to an environmental problem at their properties should resolve potential liability issues. Similarly, agreements in principle regarding the EPA's intent in particular transactions will likely be catalysts to explore other projects and transactions. Statements of policy regarding matters such as property located over contaminated groundwater will provide clarifications for property owners.

Proactive negotiation

Attitudes of responsible parties have also changed significantly, particularly where the party has substantial experience in environmental issues. The most effective companies have been seeking to reduce transaction costs by taking appropriate responsibility and settling with other interested parties in order to avoid costly litigation.

For example, we have been able to negotiate settlements involving multiple parties expeditiously, negotiate indemnities to lenders to facilitate refinancing, and obtain indemnities from or provide indemnities to tenants and occasionally owners with respect to conditions that would otherwise have created problems in transactions. In turn we have reached agreements for access, cleanup and continued monitoring — both when representing responsible parties and when representing those seeking such assurances or arrangements from responsible parties.

There has been a marked improvement in the willingness of all interested parties to seek cost-effective solutions and to work together to reach agreements that meet goals and resolve issues without litigation.

Regulatory picture

Further changes would provide more relief to the regulated community with no real downside in environmental quality. Regulatory agencies should seek to:

- Minimize affected acreage and parcels where environmental conditions require remediation. Why characterize an entire area based on a few troublesome parcels?
- Standardize remedies and approaches where possible for practicality and predictability. We do not need to reinvent the wheel on every case.
- Limit future impacts on property where issues of potential liability must be kept open. For example, do not demand wells inside buildings, and do not require open-ended, uncontrolled access, especially where the site is well understood.
- Focus on minimizing uncertainties so that transactions do not fall apart because

parties cannot get sufficient assurance of the status of a particular parcel, or a firm grip on the nature or potential cost of future actions that may be required.

■ Implement only reasonable deed restrictions, for reasonable times, using nonprejudicial, reasonable language.

■ Take meaningful steps to determine health and safety risks at early stages of site assessment, to reduce the effect of perceived risks on surrounding areas and populations, where possible.

■ Set definitive "no significant risk" levels for residual contamination, to provide cleanup guidance and assurance regarding health and safety concerns."

■ Approve, without lengthy delays or expensive revisions, reasonable, practical solutions and agreements proposed by respon-

sible parties. Focus on substance and cleanup rather than formalities and paperwork. Utilize mediation to reach settlements.

■ Expand use of mixed funding at the federal level so that the "Superfund" pays part of the cleanup costs. Use peer review panels for cleanup strategies and to set cleanup levels, promote better solutions, speed the review process and involve the community in deciding what needs to occur at a particular parcel.

In the future

We expect to see even more changes and options as environmental issues are addressed by a regulatory system, which, finally, seems to be trying to "do the right thing" and make decisions that are more logical, cost-effective and politically viable. ■

Insurance

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of property where the cleanup is required by a governmental authority or by the discovery of contamination that exceeds state or federal action levels. Policies also can be written for financial institutions to cover the loss in asset value of the outstanding balance of the real estate loan. Third-party bodily injury, property damage and cleanup cost claims may also be covered. Insurance can be for individual sites or for an entire portfolio.

Asbestos and Lead Paint Liability. This insurance covers third-party bodily injury and property damage and cleanup cost protection for claims arising out of or following asbestos and lead paint abatement activities. Insurance can be written for property owners

and/or contractors working on the owner's behalf, and may cover encapsulation of asbestos as well as removal.

Transportation, Treatment and Disposal. Coverage is written for remediation projects that involve removal of hazardous wastes and treatment and disposal. These insurance policies acknowledge and respond to a release of materials during transportation and after delivery of hazardous wastes to a disposal facility. Transportation coverage can be provided by the firm that hauls the hazardous wastes or on a policy purchased by the site owner/generator. Protection for releases from third-party disposal sites is normally written only where other environmental damage insurance is placed by the owner of the site being remediated, and typically does not pay for the cost of cleanup of the disposal site itself. ■

Renovations

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by the end of its fiscal year. The conditions of the sale were that the property could be developed without restriction to its highest and best use.

Working with the buyer's consultant, the site was investigated using test pits, borings and monitoring wells, and a remediation program was developed that included soil-vapor extraction and soil excavation/recycling into asphalt. This program was approved by the local and regional regulatory agencies.

During implementation of the remediation program, affected soils were identified within a large former landfill area on the site. The soils were impacted by heavy oils and polynuclear aromatics, or PNAs, and comprised approximately 50,000 cubic yards of material. Although the PNA concentrations were low, they exceeded certain health-risk criteria developed by the Department of Toxic Substances Control. Based on its analysis, DTSC indicated that further work must be done to evaluate and potentially remediate the PNAs. This additional work could not have been finished prior to the end of the fiscal year. The lead agency, the California Regional Water Quality Control Board, would not allow closure of the site, and therefore sale of the property without DTSC approval.

A program was implemented to look at the origin and potential risk of the PNAs more carefully. This included modifying the PNA analysis method to screen out the heavy hydrocarbon interference and basing the risk analysis on the distribution of the PNAs with respect to the grain-size distribution. It was demonstrated that the PNAs did not pose a human health risk at the site. DTSC approved the analysis and the RWQCB allowed the

closure of the site without removing the PNAs and heavy hydrocarbons. The property transaction was completed approximately two days before the end of the fiscal year.

■ **Redevelopment of a landfill.** Twenty-two-story, steel-framed commercial buildings, entrance roadways and parking areas were planned for construction as part of commercial development of a 50-acre portion of a former municipal landfill site in Northern California. Geo-environmental aspects of the development included: construction of a cap in accordance with state regulations, advancement of piles through the landfill following demonstration that the piles would not promote chemical migration to groundwater; provision of vapor barriers where appropriate to control methane migration; and continued leachate and groundwater monitoring. Strategic investigation of environmental concerns and pragmatic approaches to their resolution, coupled with the proposed site development, resulted in state approval for the development and initiation of construction in the landfill area.

Final thoughts

Although regulations are changing rapidly and there is a stated intent by government to develop properties that are affected by chemicals, it will be some time before all regulatory requirements are clarified to meet the needs of the lenders and site owners. In the meantime, creative and competent technical teams can take advantage of the increasing number of opportunities to develop or manage contaminated properties even under the current regulatory climate.

Effective project partnerships among owners, developers, attorneys, consultants, and regulators will continue to expedite the restoration of brownfield-type sites to economic health. ■

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