Why an ASTM Standard Environmental Assessment May Not Address Costly Environmental Risks

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Standard E1527-13 is a voluntary standard, published by ASTM International, for performing Phase I Environmental Site Assessments (ESAs) of commercial properties in the United States. The standard is also used to assess multi-family and industrial properties nationwide. These methods are widely recognized as industry-standard when assessing properties for Recognized Environmental Conditions (REC), and they represent a starting point from which to benchmark the environmental conditions of commercial property. The standard, however, does not address all potential environmental conditions that are important to consider when purchasing real estate. Business Environmental Risk (BER) is a term defined by ASTM and applies when an environmental condition does not meet the definition of an REC, mostly because it is a not an ASTM-required scope item to be evaluated. BERs can have a material environmental or environmentally-driven impact on the business associated with the current or planned use of a parcel of commercial real estate. These risks are site-specific and often depend on the type of property being assessed and the future property use. Financial impacts from unidentified BERs can manifest themselves or present a challenge after the property is acquired, and most financial impacts are revealed when a property is being demolished or renovated. Financial impacts may include the following:

- Indoor air quality
- Asbestos
- Lead-based paint
- Mold and moisture-intrusion
- Radon
- Other building hazardous materials
- Potential legacy environmental liabilities

Indoor Air Quality (IAQ):

IAQ issues may be indicative of Heating Ventilation, and Air Conditioning (HVAC)/ mechanical system deficiencies or problems that could be costly to repair, or which may require system replacement.

Asbestos-Containing Materials (ACM) and Lead-Based Paint (LBP):

ACM and LBP can pose other costly environmental risks if building renovation/ demolition are planned and could add unexpected costs to such projects if not contemplated during the property acquisition due diligence period. ACM and LBP may pose additional environmental risks, health and safety concerns, and/or regulatory compliance issues if the property in question is utilized for residential, hospitality, or healthcare-related purposes.

Mold/Moisture Intrusion:

Mold and moisture intrusion can be a nuisance and diminish the integrity of structural components of a building. Mold and moisture intrusion issues can be time-consuming to investigate and costly to remedy. This could also pose additional environmental, health, and safety concerns if the property is used for residential, hospitality, or healthcare-related purposes.

Radon:

Radon can also pose a significant health and safety concern, particularly to occupants of residential and/or nursing facility properties. Depending upon the concentration and extent of radon within a building, the installation, operation, and maintenance of a radon mitigation system could also represent an unplanned expense that would not necessarily have been contemplated during the course of an ASTM Phase I ESA.

Other Building-related Hazardous Materials:

The presence of other building-related hazardous materials, such as mercury-containing devices (e.g., switches, thermometers, thermostats), lead-acid batteries, fluorescent light bulbs/ballasts, and chlorofluorocarbon-containing equipment may also represent a "hidden" environmental cost in the event that building demolition or significant renovation is planned that would include the removal and proper disposal of such materials.

Potential Legacy Environmental Liabilities:

Potential legacy environmental liabilities could also be attached to a property, depending upon property use and the type of tenants occupying the property. For instance, a tenant that generates a significant amount of hazardous waste may be experiencing financial and regulatory compliance issues that would not necessarily have been identified during the completion of an ASTM Phase I ESA. If the tenant is not a financially solvent company the property owner may face costly environmental remediation and disposal costs for complying with waste-related regulatory requirements not fulfilled by their tenant.

One potential BER that can arise after acquisition is when regulated or hazardous waste is discovered during renovation or demolition. The property owner is required to dispose of building materials classified as regulated or hazardous in accordance with federal, state, and local regulations. As such, a property owner may incur costly decontamination, asbestos abatement, or lead removal costs, and can be held liable for contamination at waste disposal facilities where contaminated waste was sent before being characterized properly.

Environmental insurance can reduce the potential exposure related to BERs, but this approach can have limited success based on the risk tolerance of the carrier and the site-specific environmental information available for the property. Some carriers no longer issue environmental policies. Phase I ESAs that do not adequately identify the nature and extent of BERs may cause the carrier to exclude certain coverages, set a high self-insured retention (SIR), set sub-limits, and /or set a higher premium commensurate with the perceived risk.

While costs to perform Phase I ESAs can increase when the scope of work is augmented to include identifying BERs, it could greatly reduce post-acquisition expenditures and environmental liabilities.

Pre-closure options to mitigate the impacts of BERs include:

- Assign remediation/abatement costs (ACM, LBP, and mold) to the owner prior to close
- Require the owner to remove/dispose of hazardous building materials and hazardous waste as a condition of the sale
- Adjust the purchase price of the property to fund remediation/abatement projects and/or the removal/disposal of hazardous building materials and hazardous waste, if not performed prior to completion of purchase
- Preparation of operations and management plans related to managing ACM and LBP in-place. These plans are typically required to secure a loan or obtain environmental insurance coverage.

In light of this information, it is important for companies seeking to purchase properties to perform a comprehensive assessment that includes non-ASTM scope environmental conditions. A comprehensive assessment is a multi-disciplinary approach to understanding site-specific environmental risks and guides decision makers in identifying hidden acquisition-related cost liabilities. Discovering BERs after-the-close reduces options to divert remediation/clean-up costs and liability to other parties (current property owner). The key to managing these risks is to perform an assessment to identify BERs before closing on a property.

For further information, you can also refer to Chubb Global Risk Advisors' advisory titled *Due Diligence – 9 Steps Companies Should Take to Effectively Manage Environmental Risks in Commercial Real Estate Deals.*

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10/2019