



REAL ESTATE
COUNSELORS

It's Just a Phase: *Good reasons for buyers to order a Phase I ESA*



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WHEN BUYING CERTAIN COMMERCIAL REAL ESTATE, such as a vacant lot or industrial property, a buyer should have an experienced environmental consultant perform a Phase I Environmental Site Assessment, commonly known as a "Phase I." To prepare a Phase I, the consultant gathers information to develop an opinion about the environmental condition of the property.

The Phase I is used to identify actual or potential environmental contamination that may impact the property's value or limit its use due to regulatory mandated cleanups. A Phase I is only the initial phase of investigating the environmental condition of property. If the Phase I finds any matters of concern, additional investigation or testing may be recommended.

Some of the key reasons for performing a Phase I are discussed below.

- **Due Diligence** – Purchasers use a Phase I as a basic due diligence tool. It's a relatively inexpensive way to discover the history of the property and whether the property is a good investment. As an example, if the report comes back with a finding of a leaking oil tank underground, the purchaser could renegotiate the cost of the property and take clean-up costs into consideration. Alternatively, the purchaser could demand that the seller resolve the matter prior to sale.
- **Innocent Purchaser** – Under the right set of circumstances, a buyer of property may use a Phase I as a defense to liability for certain environmental matters. The Comprehensive Environmental Response, Compensation and Liability Act (commonly known as "CERCLA") holds property owners liable for the cleanup of hazardous substance releases on their real property.





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- **Innocent Purchase (cont.)** – CERCLA, however, includes a defense to liability for so-called “*innocent purchasers.*” If someone conducts a Phase I before they buy a property, and the report does not find any contamination, then the purchaser will have a defense to liability for any contamination because the purchaser did not have any reason to know that the property was contaminated when purchased.
- **Lender Requirements** – A buyer who is financing the acquisition of the property may be required by the lender to obtain a Phase I. Whether a lender will require a Phase I report will depend on the loan type (for instance a Fannie Mae, Freddie MAC, or HUD loan each have varying due diligence requirements), property type or other risk factors.
- **Contract Issues** – When negotiating the terms of a purchase agreement, a buyer who may want to get a Phase I (or may be required to) should make sure their study period is long enough to have the Phase I performed and that the seller agrees to permit the buyer to conduct environmental investigations (including soil samples).
- **Your Transaction** – The issues discussed in this article may not necessarily apply to your transaction, and your transaction may raise issues not addressed in this article. In all cases, we advised you to consult an experienced commercial real estate broker and experienced commercial real estate attorney to make sure the issues for your transaction are properly addressed.

