

Are buyers opting to conduct phase 2 environmental investigations, and skipping the phase 1 step? - by Chuck Merritt



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When the American Society of Testing Materials (ASTM) first issued an environmental standard in 1994, the main phrase utilized to determine if additional investigation (phase 2) was needed was “obvious signs of contamination”. Since this can be a subjective statement (like many other aspects of environmental consulting), many consultants did not believe the properties they were inspecting met this threshold, so the phase 1 was enough. Flash forward 30 years to the issuance of the current ASTM E1527-21 standard in February of 2024 and the phrase “obvious contamination” is the furthest thing away from how consultants approach writing phase 1 reports. Many phase 1 reports conducted under the new standard, are concluding with “additional investigation” is recommended leaving buyers, owners, and lenders confused.

The definition of a Recognized Environmental Condition (REC) is “the presence of hazardous substances or petroleum products in,

on, or at the subject property due to a release to the environment; (2) the likely presence of hazardous substances or petroleum products in, on, or at the subject property due to a release or likely release to the environment; or (3) the presence of hazardous substances or petroleum products in, on, or at the subject property under conditions that pose a material threat of a future release to the environment.”

There are still many situations that are easy for consultants to call out as a REC that hopefully everyone can agree with. For instance, an abandoned gasoline station with buried tanks housing different types of petrochemicals that have not been addressed. Dry-cleaning establishments that utilize the chlorinated solvent Perchloroethylene (PERC) can also be easy for the consultant to place in the REC section for their client. However, what happens when the consultant determines that the tenant has utilized environmentally friendly chemicals for the past decade? In the ASTM 1994 version, some may state that this is a mitigating factor and conclude there is no need for further investigation. Utilizing the more recent ASTM-21 standard and now knowing how dangerous PERC is, there will more likely be a phase 2 recommendation to rule out any past releases at the property. The dry-cleaning scenario gets more complicated when the usage occurs next door or down the block vs at the target property since va-

por migration of these chemicals as they volatilize allows them to travel further, potentially

through cracks in building foundations. The latest version of the ASTM standard calls this out as a concern (REC) and consultants are responding. Many lenders today have in-house environmental staff and outside vendors that are tasked with rendering an opinion on those kinds of statements. More times than not, a phase 2 may be recommended where that was not the case in the past.

So why bother with a phase 1 in the first place? For starters, it is the road map as to what may be needed next. Otherwise, the consultant is guessing on the scope of work and may not find everything. The cost of the phase 1 is relatively inexpensive compared to the cost of real estate being purchased. Lenders typically are not going to just skip a phase one as their risk policy may require it. So, you may be doing it for your lender anyway. A properly prepared phase 1 meeting the definition of All Appropriate Inquiry (AAI) will also provide some legal protection under CERCLA law and innocent landowner defense. Attorneys preparing contracts for a buyer will be familiar with the language required.

When buying land or a site to be re-developed, consideration should be given to obtaining soil/groundwater regardless of the phase 1 outcome. Once the excavation begins, should there be any environmental issues discovered, costs will escalate, regulatory

notification may be required, and construction delays will occur. Even “historic fill” material that was once easy to dispose of has become more expensive as disposal manifests are now required in many states.

Environmental consultants belong to peer and educational groups like other industries to learn and banter ideas with each other. Most understand that a report conducted under previous standards several years ago does not mean an inferior product was issued. In addition, who the client was when the report was prepared is important to understand. Since there is a degree of subjectivity, a phase 1 report commissioned by a lender during a refinance several years ago, may be different than one prepared for a buyer today whose consultant is looking through the prism of the ASTM-21 standards. Environmental due diligence is a series of steps conducted by a reputable firm (carrying proper insurance) to determine if the commercial real estate in question may have an impact caused by current or past operations at the site or neighboring properties. Buyers should anticipate several weeks for this to be completed properly and have that outlined in the contract of sale. There is a reason environmental consulting has phases.

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