



New Environmental Diligence Standards for All Appropriate Inquiries (AAI)

(a live interactive 90-Minute Teleconference Program)

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Overview of Today's Program

- **Origins of the Rule – *Peter Murphy, Washington, D.C.***
- **Key Elements of the AAI Rule – *Alan Bick, Orange County***
- **Practical Application of the AAI Rule – *Tom McHenry, Los Angeles***



Origins of the Rule: The Original Text

- **Under CERCLA Section 107(b)(3), there is no liability for the current owner of a contaminated facility if:**
 - the **release** was caused solely by a third party
 - who neither works for the defendant nor
 - is in a “contractual relationship” with the defendant



Origins of the Rule: SARA to the Rescue?

- **Congress creates “innocent purchaser defense” in response to narrow construction of the “third party defense”**
- **Current owner only has a defense to liability if it can show:**
 - it did not know and had no reason to know of preexisting contamination
 - despite making “all appropriate inquiry” into “previous ownership and use” of the facility



Origins of the Rule: What Went Wrong? Narrow Construction of “Innocence”

- **Courts read the elements of the defense strictly – rarely conferring “innocent” status**
- **In absence of clear guidance in the statute on what is required for “all appropriate inquiry,” courts often held liable property owners who appeared to have conducted rational, thorough pre-purchase environmental investigations**



Origins of the Rule: What Went Wrong?

“Left without a viable ‘innocent landowner’ defense, the prospective purchaser’s best defense is simply to refuse to buy even minimally suspect property.”

-- Topol & Snow, “Superfund Law & Procedure” 1992



Origins of the Rule: The Solution? 2002 “Brownfields Amendments”

- **The Small Business Liability Relief and Brownfields Revitalization Act of 2002**
- **Directed EPA to draft regulations regarding what constitutes “All Appropriate Inquiry” (“AAI”) for purposes of the innocent purchaser defense**



2002 “Brownfield Amendments”

- **Congress directed EPA to include in the rule:**
 - Inquiry by environmental professional
 - Interviews with past/present owners/operators
 - Review of historical sources/liens/government records
 - Visual inspection of the property
 - Consideration of purchase price adjustments
 - Sophistication of purchaser
 - Common knowledge/obviousness



Origins of the Rule: EPA Rulemaking

- **“Negotiated Rulemaking”**
- **Considerable stakeholder involvement**
 - Environmental consultants
 - Business Community
 - Environmental Public Interest Groups
- **Final Rule promulgated November 1, 2005**
 - Effective November 1, 2006



Key Elements of the AAI Rule

Alan Bick



AAI's Primary Objective

- **“Identification of conditions indicative of releases and threatened releases of hazardous substances on, at, in or to the subject property”**



Inquiry by “Environmental Professional”

- **Current P.E. or P.G. license or license to conduct environmental inquiries and have 3 years of relevant experience; or**
- **B.A. or higher in engineering or science and 5 years of relevant experience; or**
- **10 years of relevant experience.**



Interviews with Past and Present Owners, Operators & Occupants

- **Interview of the subject property's current owners or occupants is required**
- **Interview of past owners and occupants "if necessary"**
- **Interview of adjacent owners/occupants if subject property is abandoned**



Review of Historical Sources

- **Historical documents and records must be reviewed (e.g., aerial photographs, fire insurance maps, building records, chain of title documents, land use records)**
- **Sources reviewed must cover time period as far back as first land use/structure at subject property**



Review of Government Records

- **Federal, tribal, state and local government records must be reviewed**
- **Subject property: release records; records of on-site activities; CERCLIS records; public health records; records of engineering or institutional controls**
- **Adjacent/nearby properties: various records for properties within ½ or 1 mile of subject property**



Visual Site Investigations

- **Visual on-site inspection of the subject property required**
- **Visual inspection of adjoining properties required**
- **If for “unusual circumstances” on-site inspection cannot be performed, specific documentation requirements apply**



Obviousness/Detection of Contaminants

- **Must consider the “obviousness” of the presence of contamination**
- **Must consider the ability to detect contamination by appropriate investigation**
- **EP should include an opinion regarding additional appropriate investigation**



Other Elements of AAI

- **Assessment of any specialized knowledge or experience of purchaser**
- **Assessment of the relationship of purchase price to value of property, if not contaminated**
- **Searches for environmental cleanup liens**
- **Commonly known or reasonably ascertainable information**



AAI Report Requirements

- **Opinion as to any identified conditions indicative of releases**
- **Identification and evaluation of data gaps**
- **Qualifications and signature of EP**
- **Opinion regarding additional investigation if EP has such an opinion**



Timing Issues

- **AAI must be conducted within one year prior to date of acquisition of subject property**
- **Certain components of AAI must be updated after 180 days**



New AAI Standard v. Updated ASTM E1527

- **Updated ASTM E1527-05 is consistent with requirements of new AAI standard**
- **ASTM E1527-05 may be used to comply with the provisions of AAI**



Practical Application of the AAI Rule

Tom McHenry



Application of the New AAI Rule -- Outline

- Evolving “best practices” standard
- What is not included in an AAI review
- Dealing with data gaps and disclosure
- Use of consultants
- AAI costs and timing
- What do consultants think about the new AAI standard?
- Thoughts going forward



Evolving Best Practices for AAI

- **Focus on purpose of the diligence**
- **Determine client goals and expectations**
- **Most Phase I reports are “AAI Plus”, i.e. with additional components**
- **Compliance review often useful**
- **Disclosure of missing information**



“Best Practices” Development

- **New standards in effect for 5 months, since 11/1/06**
- **Most consultants familiar with new AAI standard and have been using it over past year**
- **Potential Issues**
 - Interviews
 - Review of historical sources
 - Specialized knowledge of buyer
 - Shelf life of report



Reminder: What is Not Included in AAI Diligence?

- **AAI Standards do not specifically address**
 - **Non-CERCLA federal claims**
 - **Potential liability under state law**
 - **Petroleum contamination**
 - **Asbestos**
 - **Mold**
 - **Wetlands**
 - **Land use**
 - **Compliance**



Use of Consultants

- **Need to ensure that consultant familiar with new AAI Standards**
- **Must use a “qualified professional” as defined**
- **Require consultant to obtain sufficient insurance**
- **Name client as additional insured**
- **Obtain indemnification for errors and omissions**
- **Increased costs to prepare Phase I reports**



Timing and Cost

- **Timing is everything in environmental diligence**
- **Certain aspects of AAI diligence must be updated within 180 days of acquisition**
 - Interview
 - Lien Search
 - Governments Records
- **Costs of Phase I reports will increase**



Dealing with Data Gaps

- **Consultants already advising on whether the project should be a “Full AAI” or “Partial AAI”**
- **Requirement to identify data gaps and their significance**
- **Interviews are a challenge, especially for past tenants, neighboring property owners, etc.**
- **Using a broader set of databases – historical societies**
- **Delay in obtaining governmental records**



Developing Best AAI Practices

- **Already doing so by participating in today's webcast**
- **Understand the purpose of the diligence**
- **Understand what is covered by AAI and what is not**
- **Fashion the diligence exercise accordingly**
- **Provide clear expectations to consultant**



Consultant Comments

- **“Most clients don’t care about the innocent purchaser defense.”**
- **“AAI is not changing the conclusions, just making the report more detailed.”**
- **“Cost increase is on the order of several hundred to several thousand dollars.”**
- **“Clients need to know they will see more exceptions in the Phase I reports.”**



Miscellaneous

- **Some states have additional requirements – New Jersey, Connecticut**
- **Other states offer programs to obtain greater certainty – Michigan, Texas, Pennsylvania**
- **Title review and tribal records**



Issues Going Forward

- **Foster good working relationships with consultants**
- **Develop consultant contracts and clear expectations for work product**
- **Monitor any proposed changes to standards and best practices**
- **Focus on the purpose of the diligence**



GIBSON, DUNN & CRUTCHER LLP

QUESTION AND ANSWER SESSION

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