The art of due diligence

Terminals continuing to expand without fully assessing the environmental liabilities may learn the hard way. Don’t let your terminal become the next case study, warns Gail A Corrigan, Corrigan Consulting, Inc

Environmental due diligence should be considered as a strategy during acquisitions. In spite of today’s economic downturn, many terminals are growing and expanding. Unfortunately, many terminals are in such a hurry to expand to meet current storage needs and gain market share that they don’t start the environmental due diligence process early enough and/or don’t conduct all the environmental due diligence that is warranted for a new acquisition.

Acquiring additional property or another terminal in order to expand your operations could cost you several thousand, several hundred thousand or even a million dollars in environmental remediation. In addition to the environmental remediation liabilities, you can also incur loss of operating revenue, penalties, compliance costs, permit transfer problems, and local government and public scrutiny.

Acquiring contaminated property

The environmental due diligence standards in the US have changed since 2005. There are now EPA rules and provisions to afford limitations on environmental liabilities for companies purchasing contaminated properties (‘bona fide prospective purchasers’) and for purchasing property with contamination from an off-site source (‘contiguous property owners’). But, you must meet the statutory criteria to qualify including performing ‘all appropriate inquiry’ or due diligence. You must also comply with any land use or deed restrictions, prevent any ongoing releases, provide full cooperation to authorities to conduct response actions and provide any legally required notices. These provisions can provide significant advantages for terminal expansions, considering the fact that many expansions may involve industrial properties with a high likelihood of historical contamination. But, to be eligible for these limits on liability, you must perform an appropriate level of due diligence.

What constitutes environmental due diligence?

What does environmental due diligence include? That depends on the nature of the acquisition. For the acquisition of a ‘greenfield’ property (property that has never been developed), a Phase I Environmental Site Assessment (ESA) per the ASTM Standards may be an appropriate level of due diligence. A Phase I ESA includes researching the historical use and development of the property, researching the regulated facilities located on or surrounding the property, interviewing persons familiar with the property and conducting a site reconnaissance. A Phase I ESA typically costs US$3,000 - $6,000, depending on the size and location of the property, and can be completed within three weeks. If no recognized environmental condition or potential contamination is identified, then no further investigation is warranted and the Phase I ESA will satisfy the due diligence requirements and any lending institution requirements.

For the acquisition of a ‘brownfield’ property (property that has been used for commercial or industrial activity), a Phase I ESA may only be the beginning of the due diligence process. Conducting a Phase I ESA of a brownfield property will likely uncover recognized environmental conditions (RECs). A REC is defined as the presence or likely presence of hazardous materials or petroleum products on the property that could result
In surface water, sediments, soils and/or groundwater contamination and could result in regulatory agency requirements for remediation. In which case, a Phase II ESA is necessary to fulfill the environmental due diligence requirements.

A Phase II ESA typically includes surface and/or subsurface sampling and analysis. Depending on the nature and extent of the potential contamination, a Phase II ESA typically costs $15,000 - $60,000 or more.

However, some level of environmental compliance auditing needs to be performed and should be focused on the high level issues including, at a minimum, an assessment of the current permits vs the permits needed for future operations; the regulatory status with respect to violations, penalties and fines; spill control especially in loading/unloading areas; storm water management; management of tank bottoms and wash water; maintenance records related to what you are agreeing to remediate and this could be a significant financial risk. It may also be possible to negotiate the terms of the environmental remediation requirements to exclude any liabilities for any currently documented environmental contamination.

**Case History:** During a recent acquisition, the environmental due diligence was started as soon as the contract was signed which included a 90-day assessment period. The acquisition included a 12-acre parcel as part of a storage facility expansion. The only known environmental issues that had been identified included some abandoned used tires and a pipeline metering station located on the property. Our client, the buyer, told us that the property was 'clean as a whistle'. However, during the environmental assessment, we identified an environmental issue which was going to require mitigation prior to development of the property. The buyer was then very frustrated as this environmental information presented an impediment to his facility expansion. However, he was then convinced to use this information to his benefit. The purchase price of the property was successfully renegotiated from $750,000 to $400,000, saving $350,000, which should more than cover the environmental cost.

**Environmental due diligence as an opportunity**

No one wants to find environmental problems during an acquisition, but the environmental due diligence process is an easy way to save money and avoid/limit liabilities. Most of the time, the seller is as anxious as the buyer is to make the deal happen. And, the seller is often very willing to sell at a lower cost to avoid known environmental liabilities or to provide limits on environmental liability when they know there aren’t any significant environmental problems. Don’t let someone else’s environmental liabilities become yours or, at least, know what you are signing up for in terms of environmental liabilities. Furthermore, most environmental liabilities are manageable. There are environmental regulatory programmes that can facilitate the acquisition of contaminated property. These programmes can also be utilised to manage environmental remediation cost-effectively and in a timely manner. Don’t skip the environmental due diligence process. Use it as your ally and one of your acquisition strategies.

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