

# The New “All Appropriate Inquiries” Rule

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**The EPA’s all appropriate inquiries (“AAI”) rule will impose new diligence requirements for owners and tenants.**

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**THE EPA’S** long-awaited standard for conducting environmental due diligence became effective on November 1, 2006. *Standards and Practices for All Appropriate Inquiries*, 70 Fed. Reg. 66,069 (November 1, 2005). The rule establishes specific requirements for the “all appropriate inquiries” (“AAI”) that are necessary to establish the landowner defenses under CERCLA. Recipients of brownfield grants must also comply with AAI to assess and characterize brownfield sites. For the reasons explained in this

article, it is unclear if landowners, tenants, and lenders will follow AAI when performing environmental diligence.

**BACKGROUND OF THE NEW RULE** • The Small Business Liability Relief and Brownfields Revitalization Act of 2002 (the “2002 Brownfield Amendments”), Pub. L. No. 107-118, 115 Stat. 2356 (January 11, 2002), altered the liability scheme of the Comprehensive Environmental Response, Compensation and Liability Act (“CERCLA”) in the following three ways:

- It amended the existing innocent purchaser defense;
- The legislation added the bona fide prospective purchaser (“BFPP”) defense. 42 U.S.C. §9607(r); and
- The law created a new contiguous property owner (“CPO”) defense. 42 U.S.C. §9607(q).

To assert these defenses, parties must demonstrate that they have conducted AAI into the past use and ownership of the property before taking title.

### **Statutory Criteria For AAI**

The 2002 Brownfield Amendments also required the EPA to develop regulations establishing standards and practices for conducting AAI in accordance with statutory criteria and generally accepted good commercial and customary standards and practices. The statutory criteria are set forth in CERCLA section 101(35)(B)(iii), 42 U.S.C. §9601(35)(B)(iii) and include:

- The results of an inquiry by an environmental professional;
- Interviews with past and present owners, operators, and occupants of the facility for the purpose of gathering information regarding the potential for contamination at the facility;

- Reviews of historical sources, such as chain of title documents, aerial photographs, building department records, and land use records, to determine previous uses and occupancies of the real property since the property was first developed;
- Searches for recorded environmental cleanup liens against the facility filed under federal, state, or local law;
- Reviews of federal, state, and local government records, waste disposal records, underground storage tank records, and hazardous waste handling, generation, treatment, disposal, and spill records concerning contamination at or near the facility;
- Visual inspections of the facility and of adjoining properties;
- Specialized knowledge or experience on the part of the defendant;
- The relationship of the purchase price to the value of the property, if the property were not contaminated;
- Commonly known or reasonably ascertainable information about the property;
- The degree of obviousness of the presence or likely presence of contamination at the property, and the ability to detect the contamination by appropriate investigation.

After determining that the voluntary consensus standard developed by ASTM International known as the *Standard Practice for Environmental Site Assessments: Phase I Environmental Site Assessment Process* (ASTM E1527-00) was inconsistent with the statutory criteria, the EPA convened a rulemaking committee to develop a consensus AAI standard. 70 Fed. Reg. at 66,081.

### **Interim Standard**

The 2002 Brownfield Amendments provided that persons seeking to assert the CERCLA landowner defenses would have to comply with the interim

federal AAI standard until the EPA promulgated its AAI rule. 42 U.S.C. §9601(35)(B)(iv). While a draft AAI rule was under development, the EPA clarified the interim federal AAI standard. 68 Fed. Reg. 24,888 (May 9, 2003). The agency indicated that persons who purchase or occupy property on or after May 31, 1997 would have to demonstrate that they complied with ASTM E1527-00 or the earlier 1997 version (ASTM E1527-97). For commercial property purchased before May 31, 1997, the 2002 Brownfield Amendments provided that property owners would have to establish that they complied with the statutory criteria for establishing the innocent purchaser defense that had been in effect before the 2002 Brownfield Amendments. The criteria for determining if a defendant/owner conducted an appropriate inquiry included:

- Any specialized knowledge or experience on the part of the defendant;
- The relationship of the purchase price to the value of the property, if the property were not contaminated;
- Commonly known or reasonably ascertainable information about the property;
- The obviousness of the presence or likely presence of contamination at the property; and
- The ability of the defendant to detect the contamination by appropriate inspection.

42 U.S.C. §9601(35)(B)(iv)(I).

### **The Proposed Rule**

The EPA published its proposed AAI rule in August 2004 and received more than 400 comments. 69 Fed. Reg. 52,542 (Aug. 26, 2004). While a negotiated rulemaking committee was developing the draft AAI rule, the ASTM Phase 1 Task Force began working closely with the EPA to revise the E1527-00 standard to ensure that the revised standard would satisfy the requirements of the AAI rule.

### **The Final Rule**

When the EPA issued the final AAI rule, the agency announced that E1527-05 was consistent with the final rule so that environmental site assessments consistent with ASTM E1527-05 would be considered to be in compliance with the final AAI rule. 70 Fed. Reg. at 66,081. Until the November 1, 2006 effective date of the AAI rule, persons seeking the benefit of the CERCLA landowner liability protections could continue to comply with the federal interim standard (i.e., ASTM E1527-00) or could begin to implement the AAI rule or ASTM E1527-05.

This article reviews the principal components of the AAI rule and discusses the subtle differences between AAI and the ASTM E1527 standard. Before reviewing the AAI rule, it is important to note that the AAI rule addresses only one of the pre-acquisition obligations that parties must satisfy to assert the CERCLA landowner defenses; it does not address or satisfy the numerous post-acquisition continuing obligations that landowners must comply with to preserve their liability protection. Additionally, the AAI rule does not create new reporting or disclosure obligations.

### **REVIEW OF CERCLA LANDOWNER LIABILITY DEFENSES**

• When CERCLA was enacted in 1980, it contained three affirmative defenses: Act of War; Act of God; and the third-party defense. 42 U.S.C. §9607(b). The most commonly asserted defense is the third-party defense. To qualify for this defense, a defendant must establish the following four elements:

- The release was caused solely by the act or omission of a third party;
- The defendant had no direct or indirect contractual relationship with the third party;
- The defendant exercised due care with respect to the hazardous substances (“due care element”) and;

- The defendant took precautions against the foreseeable acts or omissions of any such third parties (“precautionary element”).

42 U.S.C. §9607(b)(3).

### **Innocent Purchaser Defense**

Because a lease or purchase agreement could be considered a “contractual relationship,” the third-party defense was largely unavailable to purchasers or tenants of contaminated property. As a result, Congress enacted the innocent purchaser defense in 1986. Under this defense, a purchaser who “did not know or had no reason to know” of contamination would not be liable as a CERCLA owner or operator. 42 U.S.C. §9601(35)(A). To establish that it had no reason to know of the contamination, a defendant must demonstrate that it took “all appropriate inquiries...into the previous ownership and uses of the facility in accordance with generally accepted good commercial and customary standards and practices....” 42 U.S.C. §9601(35)(B)(i)(I). In determining whether there was an “appropriate inquiry,” CERCLA required that any specialized knowledge or experience of the innocent purchaser must be taken into account as well as the relationship of the purchase price to the value of the property if it were not contaminated, and whether the presence of contamination was obvious or could be detected by an appropriate site inspection.

Since it relies on an affirmative defense, the innocent purchaser had the burden of establishing that it satisfied the elements of the defense. Most courts narrowly construed the innocent purchaser defense. If a purchaser did not discover contamination before taking title but contamination was subsequently discovered, courts generally concluded that the purchaser did not conduct an adequate inquiry and, therefore, could not avail itself of the defense.

Further complicating the burden of the purchaser was that CERCLA did not establish specific

requirements for what constituted an appropriate inquiry. To fill this gap, the ASTM promulgated its E1527 standard.

The 2002 Brownfield Amendments add the following obligations that a landowner must comply with *after acquiring the property* to preserve its status as an innocent purchaser:

- Cooperate, assist, and provide access to persons that are authorized to conduct response actions or natural resource restoration at the property;
- Comply with any land use restrictions established or relied on in connection with the response action at a vessel or facility and must not impede the effectiveness or integrity of any institutional control employed at the vessel or facility in connection with a response action; and
- Provide access to persons authorized to conduct response actions at the facility to operate, maintain, or otherwise ensure the integrity of land use controls that may be a part of a response action.

### **Bona Fide Prospective Purchaser Defense**

Perhaps the principal drawback of the CERCLA innocent purchaser defense was that a purchaser had to establish that it had no reason to know that the property was contaminated. Because the problem with brownfields is the existence or suspicion of contamination, the defense was largely unavailable to prospective developers or tenants of brownfield sites.

To eliminate this obstacle to redeveloping brownfields, the 2002 Brownfield Amendments created a new BFPP defense. 42 U.S.C. §9607(r). This defense allows a landowner or tenant to knowingly acquire or lease contaminated property after January 11, 2002 without incurring liability for remediation if it could establish the following by a preponderance of the evidence:

- All disposal of hazardous substances occurred before the purchaser acquired the facility. 42 U.S.C. §9601(40)(A);
  - The purchaser conducted an “all appropriate inquiry.” 42 U.S.C. §9601(40)(B);
  - The purchaser complied with all release reporting requirements. 42 U.S.C. §9601(40)(C);
  - The purchaser took “appropriate care” by taking reasonable steps to stop any continuing release, prevent any threatened future release; and prevent or limit human, environmental, or natural resource exposure to any previously released hazardous substance. 42 U.S.C. §9601(40)(D);
  - The purchaser cooperated, assisted, and provided access to persons authorized to conduct response actions or natural resource restoration at the property. 42 U.S.C. §9601(40)(E);
  - The purchaser complies with any land use restrictions established as part of a response action and did not impede the effectiveness or integrity of any institutional control used at the site. 42 U.S.C. §9601(40)(F);
  - The purchaser must also provide access to persons authorized to conduct response actions to operate, maintain, or otherwise ensure the integrity of land use controls at the site. *Id.*;
  - The purchaser complies with any the EPA request for information or administrative subpoena issued under CERCLA. 42 U.S.C. §9601(40)(G);
  - The purchaser establishes that it is not a potentially responsible party (“PRP”) or affiliated with any other PRP for the property through any direct or indirect familial relationship, any contractual or corporate relationship, or as a result of a reorganization of a business entity that was a PRP. 42 U.S.C. §9601(40)(H).
- provides liability protection to a person owning property that has been contaminated by a release or threatened release of a hazardous substance from a contiguous or adjacent property. To assert the defense, the owner must establish the following by a preponderance of the evidence:
- The owner has not caused, contributed, or consented to the release or threatened release. 42 U.S.C. §9607(q)(1)(A)(i);
  - The owner is not a PRP or affiliated with any other PRP for the property through any direct or indirect familial relationship, a contractual or corporate relationship, or the result of a reorganization of a business entity that was a PRP. 42 U.S.C. §9607(q)(1)(A)(ii);
  - The owner has taken reasonable steps to stop any continuing release, prevent any threatened future release, and prevent or limit human, environmental, or natural resource exposure to any hazardous substance released on or from property owned by that person. 42 U.S.C. §9607(q)(1)(A)(iii). (The statutory language does not refer to “appropriate care” but the standard is identical to the “appropriate care” provisions in the BFPP and innocent purchaser defenses);
  - The owner cooperated with, assisted, and provided access to persons that are authorized to conduct response actions or natural resource restoration at the property. 42 U.S.C. §9607(q)(1)(A)(iv);
  - The owner has complied with any land use restrictions established as part of response action at the site and has not impeded the effectiveness or integrity of any such institutional control. In addition, the owner must provide access that is necessary to allow persons authorized to conduct response actions to operate, maintain, or otherwise ensure the integrity of land use controls. 42 U.S.C. §9607(q)(1)(A)(v);

### **Contiguous Property Owner Defense**

The 2002 Brownfield Amendments also added the CPO defense. 42 U.S.C. 9607(q) This defense

- The owner has complied with all release reporting requirements and other required notices regarding the discovery or release of any hazardous substances at the facility. 42 U.S.C. §9607(q)(1)(A)(vii);
- The owner has complied with any EPA request for information or administrative subpoena issued under CERCLA. 42 U.S.C. §9607(q)(1)(A)(vi); and
- The owner conducted an “appropriate inquiry” at the time it acquired title to the property and did not know or have no reason to know that the property was or could be contaminated by a release or threatened release of hazardous substances from other real property not owned or operated by the owner. 42 U.S.C. §9607(q)(1)(A)(viii).

An owner that cannot qualify for the CPO defense because it did not conduct an appropriate inquiry might still be able to qualify for the BFPP defense. S. Rep. No. 107-2, at 9 (Mar. 12, 2001). The owner might also be able to raise other defenses to liability that may be available under any other law. 42 U.S.C. §9607(q)(2). The EPA is also authorized to issue assurance to a contiguous property owner that no enforcement action will be initiated under CERCLA and to provide protection against claims for contribution or cost recovery. 42 U.S.C. §9607(q)(3).

#### **KEY DEFINITIONS OF THE AAI RULE •**

The AAI rule adds new definitions to the environmental due diligence process. Following are some of the more significant new terms that lawyers and consultants will have to understand.

#### **Abandoned Property**

“Abandoned property” refers to real property that can be presumed to be deserted, or when an intent to relinquish possession or control can be inferred from the general disrepair or lack of ac-

tivity thereon, such that a reasonable person could believe that there was an intent on the part of the current owner to surrender rights to the property. 40 C.F.R. §312.10(b). As discussed below, the AAI rule requires more detailed inquiries when the environmental site assessment involves abandoned property.

#### **Adjacent Property**

“Adjacent property” refers to real property that shares a portion of or an entire common boundary with the parcel being investigated or that would share a common boundary but for a street, road, or other public thoroughfare separating the properties. *Id.* As discussed below, the AAI rule mandates minimum investigative activities for adjacent properties.

#### **Data Gap**

A “data gap” refers to a lack of or inability to obtain information required under the AAI rule despite good faith efforts by the environmental professional or the person seeking the benefit of the landowner liability defenses. *Id.* This term differs from the concept of “data failure” in the E1527 standard. Data failure means that a particular historical source was not reasonably ascertainable. One of the more common examples is when consultants cannot trace historical use of a property back to 1940. Under section 7.3.2 of E1527-00, the consultant should indicate whenever there is a data failure but, because other information was available, the data failure was not critical and thus did not prevent the consultant from determining that there was no evidence of releases of hazardous substances.

#### **Environmental Professional**

This definition was perhaps the most contentious issue during the development of the AAI rule. The AAI rule requires that the inquiry be performed and documented by an “environmental professional”

(“EP”), which is defined as a person who possesses sufficient specific education, training, and experience necessary to exercise professional judgment to develop opinions and conclusions regarding conditions indicative of releases or threatened releases on, at, in, or to a property. 40 C.F.R. §312.10(b). To qualify as an EP, the person must satisfy the following minimum requirements:

- Hold a current Professional Engineer’s (P.E.) or Professional Geologist’s (P.G.) license or registration and have the equivalent of three years of full-time relevant experience, or hold a license or certification from the federal government, a state, tribe, or U.S. territory to perform environmental site assessments and have the equivalent of three years of full-time relevant experience; or
- Hold a Baccalaureate or higher degree from an accredited institution of higher education in a discipline of engineering or science and the equivalent of five years of full-time relevant experience; or
- Have the equivalent of 10 years of full-time relevant experience.

*Id.* The AAI rule provides that individuals not meeting the definition of an EP may still participate in the AAI process provided the work of the non-EP is done under the supervision of an individual that meets the regulatory definition of an EP and the EP reviews the results of the work and conclusions. The EP is required to sign the final report. *Id.*

ASTM E1527-05 adopts the AAI definition of EP and does not specify specific tasks that the EP must perform. However, 1527 does state that at a minimum the EP must be involved in the planning of the site reconnaissance and interviews and also establishes qualifications for the individual conducting the site visit and interviews.

**COMPONENTS OF AN AAI** • Any public or private party seeking to establish one of the CERCLA landowner liability protections must comply with the following elements of the AAI rule. In addition, parties awarded brownfield assessment grants must conduct site assessments and characterization activities in compliance with the AAI rule.

### **Interviews With Past And Present Owners, Operators, And Occupants**

The first statutory criterion for AAI is interviews with the current owners, operators, and occupants of the property. The AAI rule requires these interviews when necessary to collect information on past uses and ownerships of the property, and to identify potential conditions that may indicate the presence of releases or threatened releases of hazardous substances at the subject property. 40 C.F.R. §312.23. (The ASTM E1527-00 standard did not require interviews of past owners or occupants of a property but instead suggested that current owners be questioned about past uses and ownership.) If the property has multiple occupants, the inquiry of the EP shall include interviewing major occupants, as well as those occupants likely to use, store, treat, handle, or dispose of hazardous substances, or those who have likely done so in the past. 40 C.F.R. §312.23(b). The final rule also provides that additional interviews with current and past facility managers, past owners, operators, or occupants of the property, and employees of past and current occupants of the subject property, may be necessary to meet the objectives of the rule. 40 C.F.R. §312.23(c).

A significant change from the ASTM E1527 standard involves abandoned properties. When the property being investigated is abandoned and there is evidence of potential unauthorized uses or uncontrolled access, the AAI rule requires interviews with owners and occupants of neighboring and nearby properties.

## **Review Of Historical Sources Of Information**

Perhaps the single most important step in environmental due diligence is to ensure that a comprehensive historical investigation of the property is performed. Because this can be a time-consuming and costly activity, many of the lower priced Phase 1 firms will give short shrift to historical reviews.

Under section 7.3.2 of ASTM E1527-00, consultants were required to review historical records back to 1940 or to the property's first obvious use, whichever is earlier. The standard also required research intervals of not more than five years unless the property use remains unchanged. This requirement was a useful hammer to ensure that consultants adequately documented the prior use of the property.

Unfortunately, the AAI rule eliminated the minimum objective criteria that had been required by the ASTM E1527-00, such as minimum five-year intervals and reviewing historical records back to 1940 or the first use, whichever is earlier. Instead, the AAI rule simply provides that historical sources should be reviewed back to the time that the property first contained structures or was used for residential, agricultural, commercial, industrial, or governmental purposes. 40 C.F.R. §312.24(b). Under the final rule, the EP should exercise its judgment when determining the appropriate research interval or how far back to research historical records. For example, if a property was first used in 1960, the ASTM E1527 standard would require the EP to review historical sources of information going back to 1940. By contrast, under the AAI rule, historical sources of information must be reviewed only as far back as 1960.

Like the ASTM standards, the AAI rule does not require reviewing any specific historical document, nor does it specify the minimum number of records to be reviewed. Instead, it provides a list of the records that may be reviewed, such as aerial photographs, fire insurance maps, building depart-

ment records, chain of title documents, and land use records.

## **Searches For Recorded Environmental Cleanup Liens**

The AAI rule requires that the environmental site assessment include searches for cleanup liens that are filed or recorded against the property. 40 C.F.R. §312.25(a). The existence of a cleanup lien can be of particular importance to lenders if the property is located in a state that has adopted a superlien law that allows the state to file a lien for its cleanup costs that will subordinate a previously perfected security interest.

The AAI also differs from the ASTM E1527-05 standard with respect to the party responsible for conducting the search for environmental cleanup liens. Under ASTM E1527-05, the user or prospective property owner is responsible for the environmental cleanup lien search and is required to provide the results of the search to the EP. 40 C.F.R. §312.25(b). In contrast, either the prospective property owner or the EP may conduct the search. 40 C.F.R. §312.22(a)(1). Indeed, if the EP is not instructed to conduct a cleanup lien search, the person seeking the liability protection is required to perform the lien search. (However, the prospective purchaser is not required to disclose the information about the cleanup lien to the EP. 40 C.F.R. §312.25(b).) The EPA's rationale for this position is that because it is the landowner who will have to assert the defense to CERCLA liability, the landowner should not be obligated to provide this information to the EP. If the lien search is performed by the prospective property owner and it does not provide the search results to the EP, the EP should assess the impact of the missing information and determine if it represents a data gap, and should comment on the effect of the data gap on its ability to identify conditions indicative of releases or threatened releases. 40 C.F.R. §§312.20(g); 312.21(b).

### **Reviews of Federal, State, Tribal, And Local Government Records**

Like ASTM E1527, the AAI rule requires that the environmental site assessments include a review of federal and state government records and specifies the minimum search distance for each record. The AAI rule goes beyond the ASTM standard by mandating the review of local and tribal records. 40 C.F.R. §312.26(a). The E1527 standard leaves review of local records to the discretion of the EP.

In the case of federal and state government records, the type of records, and the minimum search distances do not differ significantly from the requirements included in the ASTM E1527-00 standard. Both the ASTM E1527-00 standard and the AAI rule allow the EP to exercise discretion to modify the minimum search distance for a particular record type, based upon enumerated factors. 40 C.F.R. §312.26(d). The ASTM E1527-00 standard does not allow for the reduction of search distance for the federal NPL site list and the federal RCRA TSD list. The reason or reasons for any such modification must be documented in the written report.

Because compliance with institutional controls (“IC”) and engineering controls (“EC”) is one of the elements that must be satisfied to assert the landowner liability protections, it is not surprising that the AAI rule requires identification of institutional controls as part of the search of state and local records. 40 C.F.R. §312.26(b)(7). The AAI rule requires that registries or publicly available lists of ICs and ECs be searched for the property. (The EPA has suggested prospective landowners, grantees, and EPs may want to request information on “restrictions of record on title” when requesting information on ICs or ECs about a property.) The EPA did not adopt the requirement in the proposed rule to conduct searches of ICs and ECs at properties within a half mile of the property.

The EPA decided to maintain the requirement that neighbors be interviewed in the case of abandoned properties. In addition, no changes were

made to the treatment of data gaps, the use of sampling and analysis, and determining the fair market value of the subject property. The IC and EC search may be performed by either the prospective property owner or the EP. 40 C.F.R. §312.20(e). If the search is performed by the prospective property owner and the results of the search are not provided to the EP, the EP should treat the lack of information as a data gap and should comment on the significance of the data gap on his or her ability to identify conditions indicative of releases or threatened releases.

It is important that the client and its counsel ensure that the EP has adequately reviewed local records, interviewed local officials, and used appropriate time intervals when researching historical information. This issue is particularly important at commercial properties such as older shopping centers that may have had a significant turnover in tenants. For example, the average dry cleaner operates for only three years. Thus, an EP who uses a 10-year interval may not identify a dry cleaner that formerly operated at a shopping center.

### **Visual Inspections Of The Facility And Adjoining Properties**

As with the ASTM E1527 standard, the AAI rule requires that the environmental site assessment include an on-site visual inspection of the property. Unlike E1527, though, the AAI rule allows for a waiver of the on-site inspection if it cannot be performed because of “unusual circumstances” such as physical limitations, remote and inaccessible location, or other inability to obtain access to the property. A good faith effort must be made to obtain access. (The EPA defined “good faith effort” as “the absence of any intention to seek an unfair advantage or to defraud another party; an honest and sincere intention to fulfill one’s obligations in the conduct or transaction concerned.” 40 C.F.R. §312.10(b).) An on-site inspection will not be required provided the EP:

- Visually inspects the property via another method (for example, aerial imagery) or from an alternate vantage point (for example, walking the property line);
- Documents efforts taken to gain access to the subject property;
- Documents the other information sources used to determine the existence of potential environmental contamination; and
- Expresses an opinion about how the lack of an on-site visual inspection affected the EP's ability to identify conditions indicative of releases or threatened releases.

40 C.F.R. §312.27(c). The ASTM E1527 Task Group did not include the exception because of concern that it could lead to abuse. The AAI rule expressly provides that mere refusal of a voluntary seller to provide access to the property would not constitute the kind of "unusual circumstance" that would allow waiver of the on-site inspection requirement. If a prospective purchaser or grantee cannot gain access to a site before taking title, the EPA strongly recommended that the property owner conduct an on-site visual inspection of the property after it is acquired so that it could fully comply with the other provisions of the CERCLA landowner liability protections. 70 Fed. Reg. at 66,096.

What is different is that the AAI rule also requires the EP to perform a visual inspection of adjoining properties from the subject property line, public rights-of-way, or another vantage point. 40 C.F.R. §312.27(a)(2). The EPA stated that the visual inspections of adjoining properties must include observing areas where hazardous substances currently may be, or previously may have been, stored, treated, handled, or disposed. The EP is required to document physical limitations preventing visual inspections of adjoining properties. 70 Fed. Reg. at 66,096.

Because the EPA believes that the site visit may be the single most important task of AAI, it strongly

recommended that the EP conduct the visual inspections of the property and adjoining properties. 70 Fed. Reg. at 66,097.

### **Specialized Knowledge Or Experience Of The Defendant**

This criterion was part of the original 1986 innocent purchaser defense. Under the ASTM E1527-05 standard, a prospective property owner is required to disclose to the EP any specialized knowledge of the subject property and surrounding areas that is material to recognized environmental conditions in connection with the subject property.

The AAI rule retains this requirement and provides that AAI will not be considered complete unless the investigation takes into account any specialized knowledge held by the prospective property owner. 40 C.F.R. §312.28(a). The EPA recommends that the prospective purchaser provide any specialized knowledge it may have to the parties performing the pre-acquisition inquiry. 70 Fed. Reg. at 66,098. However, the prospective property owner is not required to provide this information to the EP. 40 C.F.R. §312.22(a)(2). If the information is not provided to the EP, the EP should treat the lack of information as a data gap and should comment on how the data gap affected its ability to identify conditions indicative of releases or threatened releases. 40 C.F.R. §§ 312.20(g); 312.21(b).

The EPA did caution that the question of whether or not the AAI standard is met with regard to specialized knowledge will remain within the discretion of the federal courts. 70 Fed. Reg. at 66,098.

### **Relationship Of The Purchase Price To The Value Of The Property If Uncontaminated**

This criterion was also part of the original innocent purchaser defense. The ASTM E1527 standard requires consideration of the relationship of the purchase price and the fair market value of

the property in an uncontaminated condition only when the purchaser has actual knowledge that the purchase price was significantly less than that of comparable properties. The purchaser has to identify an explanation for the difference between price and value, and make a written record of such an explanation. However, E1527 does not specifically state that the purchaser should give this information to the EP. The EP's final report must note if the purchaser provided any of this information to the EP.

The AAI rule provides that the person seeking the landowner liability protection *must* consider if the difference in purchase price and fair market value is due to the presence of releases or threatened releases of hazardous substances. 40 C.F.R. §312.29(a). If the purchase price does not reasonably reflect the fair market value of that property in an uncontaminated condition, the purchaser must consider whether or not the differential in purchase price and fair market value is due to the presence of releases or threatened releases of hazardous substances. 40 C.F.R. §312.29(b).

If an EP is not qualified to consider the relationship of the purchase price to the value of the property, the prospective purchaser or grantee may undertake the task or hire another third party to make the comparison of price and fair market value and consider whether any differential is due to potential environmental contamination. 70 Fed. Reg. at 66,099.

The EPA indicated that a real estate appraisal is not required for the prospective purchaser or grantee to make a general determination of whether the price paid for a property reflects its fair market value. If a formal appraisal is not available, the EPA said that the determination of fair market value may be made by comparing the price paid for a particular property to prices paid for similar properties located in the same vicinity as the subject property, or by consulting a real estate expert familiar with properties in the general locality and

who may be able to provide a comparability analysis. The agency stated that the objective is not to ascertain the exact value of the property, but to determine whether or not the purchase price paid for the property generally reflects its fair market value. Significant differences in the purchase price and fair market value of a property should be noted and the reasons for any differences also should be noted. *Id.* Indeed, the agency noted that the results of a formal property appraisal may serve as an excellent source of information on the fair market value of the property.

If the person seeking the landowner liability protection does not provide information regarding the relationship of the purchase price of the subject property to its fair market value to the EP, the EP should treat the lack of such information as a data gap and should comment on the effect that the data gap may have on its ability to identify conditions indicative of releases or threatened releases. 40 C.F.R. §§312.20(g); 312.21(b).

### **Commonly Known Or Reasonably Ascertainable Information About The Property**

This criterion was also a part of the original 1986 innocent purchaser defense. Under the AAI rule, the prospective property owner and EP are required to take into account commonly known or reasonably ascertainable information about the subject property. 40 C.F.R. §312.30(a). In addition to the information sources consulted during the conduct of the historical records searches, the review of government records, and the required interviews, such information may be obtained from a variety of sources, including newspapers, local government officials, community organizations, and websites, among others. 40 C.F.R. §312.30(c). Commonly known and reasonably ascertainable information must be pursued to the extent necessary to achieve the objectives and performance factors of the final rule.

Because there has been some case law under the innocent purchaser defense interpreting the meaning of this criterion, the EPA did caution that courts will have the ultimate say on what conditions will be construed as being commonly known or reasonably ascertainable. 70 Fed. Reg. at 66,100.

***Degree Of Obviousness Of The Presence Or Likely Presence Of Contamination At The Property, And The Ability To Detect The Contamination By Appropriate Investigation***

The 1986 version of the innocent landowner defense required a court to consider the degree of obviousness of the presence or likely presence of contamination at a property and the ability of the defendant (i.e., the landowner) to detect the contamination by appropriate investigation. Persons conducting AAI must consider all the information collected during the conduct of the inquiries in totality to ascertain the potential presence of a release or threatened release at the property. After collecting all the required information, the person must assess if it is obvious that there are conditions indicative of a release or threatened release of hazardous substances (or other pollutants, contaminants, petroleum or petroleum products, and controlled substances for brownfield sites) at the property.

In addition, the AAI rule requires parties to consider if the totality of information collected before acquiring the property indicates that the parties should be able to detect a release or threatened release at the property. As part of this requirement, the EPA indicated that person performing the inquiry should consider information already obtained during the conduct of AAI and not as a requirement to collect additional information. In addition, the EP should provide an opinion regarding whether or not additional investigation is necessary to detect potential contamination at the site, if in his or her opinion there are conditions that

indicate releases or threatened releases of hazardous substances. 70 Fed. Reg. at 66,101.

These requirements are consistent with the ASTM E1527-00 requirements. However, the AAI rule went beyond the ASTM standard by requiring that the EP also provide in the written report an opinion regarding additional appropriate investigation that may be necessary, if any. The opinion could include activities or considerations outside the scope of the AAI investigation that might help the prospective property owner to more fully characterize environmental conditions on the property. The ASTM E1527-00 standard does not explicitly require that such an opinion be included in the final report.

The EPA noted that despite the conclusions of a Phase I report, a court could determine that a party is not entitled to one of the landowner liability defenses when the court finds that a preponderance of evidence available to a prospective landowner before acquiring the property indicated that the defendant should have concluded that there was a high likelihood of contamination at the site. 70 Fed. Reg. at 66,101.

**USING EXISTING REPORTS** • A party seeking to assert one of the CERCLA landowner liability protections must complete its environmental site assessment within one year of taking title to the property. 40 C.F.R. §312.20(a). Because of the increasing use of auction sales and truncated diligence periods in which purchasers have to rely on environmental due diligence materials provided by sellers, the EPA was urged to allow prospective purchasers to rely on previous reports. In addition, there was some case law suggesting that persons seeking to assert the landowner liability protections could not rely on reports prepared by third parties. *XDPI, Inc. v. Watumull Properties Corp.*, 2004 WL 1103023 (D. Or. May 14, 2004). At the same time, the EPA received comments that the one-year shelf life would be burdensome to complicated real estate developments that

take more than a year to close because the purchaser would be required to complete its due diligence before making a final decision that it actually wanted to acquire the property.

As a result, the final rule allows prospective purchasers to use previously completed Phase 1 environmental site assessment reports under certain circumstances. First, purchasers may use reports prepared within 180 days before the date of acquisition of the property that otherwise comply with the AAI rule.

Second, reports older than six months may be used provided that the following AAI components are updated to ensure that the report accurately reflects the current environmental conditions at a property:

- Interviews with past and present owners, operators, and occupants. 40 C.F.R. §312.23;
- Searches for recorded environmental cleanup liens. 40 C.F.R. §312.25;
- Reviews of federal, tribal, state, and local government records. 40 C.F.R. §312.26;
- Visual inspections of the facility and of adjoining properties. 40 C.F.R. §312.27; and
- The declaration by the EP. 40 C.F.R. §312.21(d).

Third, when the updated report is using previously collected information, the report prepared for the proposed purchase must include a summary of any relevant changes to the conditions of the property and any specialized knowledge of the prospective landowner.

In addition, the final rule also provides that under certain circumstances, a prospective landowner or brownfield grantee may use an AAI-compliant report conducted by or for another party; for example, such as when the federal government or a state government agency conducts the AAI for a property being purchased by a local government. Another situation may occur when a state government

covers the cost of the AAI for a property owned by a local government or actually conducts the AAI itself because it does not have access to appropriate staff or capital resources. Likewise, a local government or local redevelopment agency may conduct AAI on behalf of a private developer. In all cases, the prospective landowner or grantee must update the report to include commonly known and reasonably ascertainable information, relevant specialized knowledge held by the prospective landowner and the EP, and the relationship of the purchase price to the value of the property. 70 Fed. Reg. at 66,085.

Finally, the AAI rule allows information collected from previous AAI-compliant investigations to be used as a source of information even when it is more than a year old, provided that all the information is reviewed for accuracy and is updated to reflect current conditions and current property-specific information. The EPA emphasized that it is not sufficient to simply adopt a previously conducted AAI for the same property without any review. The reason is that some components of the AAI rule are likely to be transaction-specific, such as the specialized knowledge of the purchaser, relationship of the current purchase price to the value of the property, and commonly known or reasonably ascertainable information about the property. 70 Fed. Reg. at 66,084.

**DOCUMENTING THE AAI** • The goal of environmental site assessments performed pursuant to the ASTM E1527 standard is to determine the existence of “recognized environmental conditions” or “RECs.” Both E1527-05 and E1527-00 define RECs as conditions that indicate an existing release, a past release, or a material threat of a release of a hazardous substance or petroleum into structures on the property or the environment. The standard then goes on to define a “de minimis condition as circumstances that do not present a threat to human health or the environment and would generally not be the subject of an enforcement ac-

tion if brought to the attention of appropriate government agencies.” ASTM E1527-05 §3.2.74.

The EPA considered adopting the REC terminology of E1527 in the AAI rule to promote consistency but learned that the REC term was copyrighted and ASTM International reportedly would not grant permission to the EPA to use that term in the rule. Therefore, the AAI rule requires the EP to identify releases and threatened releases of CERCLA hazardous substances that cause or threaten to cause the incurrence of response costs. 40 C.F.R. §312.1(c). However, the preamble to the AAI rule also mentions that EPs are not required to identify small quantities or amounts of contaminants that do not pose a threat to human health or the environment. 70 Fed. Reg. at 66,089. Thus, except for releases of petroleum, the ASTM E1527 standard and AAI rule are functionally similar in scope.

The EP is required to issue a written report documenting the results of the inquiry. The report must include the following:

- An opinion as to whether the inquiry has identified conditions indicative of releases or threatened releases of hazardous substances (and releases of pollutants, contaminants, petroleum and controlled substances if required under a brownfield cooperative agreement). 40 C.F.R. §312.21(c)(1);
- Identification of data gaps that affect the ability of the EP to identify conditions indicative of releases or threatened releases as well as the effect of such data gaps on the EP’s ability to assess the presence of releases or threatened release. 40 C.F.R. §312.21(c)(2);
- The qualifications of the EP. 40 C.F.R. §312.21(c)(3); and
- A declaration that the AAI investigation was carried out in accordance with the requirements of the final rule. 40 C.F.R. §312.21(d).

### **WHEN IS ADDITIONAL INVESTIGATION OR SAMPLING REQUIRED?**

• One of the more vexing aspects of the due diligence process for consultants, lawyers, and clients is when further investigation is required or should be recommended. If a consultant indicates that further investigation is advisable or necessary, it will be difficult for a purchaser of property to assert that it has conducted and completed an AAI. Indeed, the overwhelming majority of cases interpreting the innocent landowner defense have ruled that if the defendant did not discover contamination, it did not conduct an AAI.

The preamble to the AAI rule specifically states that sampling and analysis is not required for an investigation to satisfy AAI but then provides a number of caveats. 70 Fed. Reg. at 66,101. However, the EPA goes on to say that sampling and analysis may be valuable in determining the possible presence of potential contamination at a property or the obviousness or extent of the contamination. The EPA also indicates that sampling and analysis may help explain existing data gaps. 40 C.F.R. §312.20 (g). Moreover, the EPA emphasized that the pre-acquisition AAI is only one requirement of the CERCLA landowner liability protections. The EPA said that sampling may be valuable for determining how a landowner may best fulfill its post-acquisition continuing obligations and that prospective landowners should be mindful of their need to comply with their post-acquisition continuing obligations when considering whether to conduct sampling and analysis. 70 Fed. Reg. at 66,102.

Depending on site-specific circumstances and the totality of the information collected during the AAI, the EPA warned that it may be necessary to conduct sampling and analysis, either pre- or post-acquisition, to fully understand the conditions at a property, and fully comply with the statutory requirements for the CERCLA liability protections. The EPA also cautioned that the fact that the AAI does not require sampling would not prevent a

court from concluding that, under the circumstances of a particular case, sampling should have been conducted to meet “the degree of obviousness of the presence or likely presence of contamination at the property, and the ability to detect the contamination by appropriate investigation” criterion and obtain protection from CERCLA liability. 70 Fed. Reg. at 66,101.

Phase 1 reports frequently recommend additional investigation such as a Phase 2 when contamination is suspected or identified. However, E1527 provides that an opinion requiring additional investigation should be provided only “in the unusual circumstance” in which the EP is unable to determine if there are RECs or when greater certainty is required with respect to an identified REC. Under this strict reading, once an EP is able to identify a REC, no further investigation is required for the purpose of satisfying the AAI requirement. This is because the ASTM definition of a REC is “the presence or likely presence of any hazardous substance or petroleum products under conditions that indicate an existing release, a past release, or a material threat of a release of any hazardous substance or petroleum products into structures on the property or into the ground, groundwater or surface water of the property.” ASTM E1527-05 §3.2.74.

In other words, once a consultant documents that there is contamination from a leaking underground storage tank (“UST”), E1527 does not *require* the consultant to provide an opinion whether further investigation is appropriate. Because such information may not be enough for the client to satisfy its continuing obligation to exercise “appropriate care” or take reasonable steps to prevent an ongoing release, a client concerned about preserving its liability defense or desiring greater certainty about the cost to remediate the REC may desire additional information. However, complying with continuing obligations is beyond the scope of AAI and is more an issue of the risk tolerance of the client. An ASTM task force on appropriate care/

continuing obligations is currently working on a standard to address this issue.

A more difficult question may be when the environmental site assessment confirms, for example, that there is an inactive UST in the ground that was installed 30 years ago. Based on his or her professional judgment and experience, and without having to render an opinion about the need for additional investigation, a consultant could conclude that the UST would probably have leaked and that contamination was “likely present” and therefore a REC. Again, a client concerned about being second-guessed by a court about the “obviousness” of the contamination or satisfying a lender may want to pursue further investigation.

The ASTM REC definition also applies to hazardous substances or petroleum products under conditions that are in compliance with laws. For example, assume that a dry cleaner has operated at a site for 20 years, a Phase 1 report states that the dry cleaner is in compliance with current best management practices (closed-loop system, sealed floor, secondary containment), but that no information is available for the prior 15 years of operation. Because prior EPA studies have indicated that 90 percent of dry cleaners in operation before 1990 likely released solvents into the environment, the consultant could conclude that there is a likely presence of a release of a hazardous substance constituting a REC without having to provide an opinion about the appropriateness of performing additional investigation.

In many ways, the preamble to the AAI rule makes it difficult for EPs, lawyers, and their clients to have confidence that they have completed an AAI. Some have argued that a property owner can be deemed to have completed AAI even if the environmental consultant states that it cannot conclude if there has been a release at the site and that further information would be required to determine if a release has in fact occurred. The argument is that once the EP has rendered its opinion, AAI is completed

for purposes of the pre-acquisition obligations of the landowner liability protections. Of course, if the landowner does not develop enough information about the release, it could lose its liability protection. However, this interpretation would not seem to be consistent with the overwhelming case law that basically holds that a landowner who did not find contamination did not conduct an AAI.

The decision whether to proceed to a Phase 2 may hinge on what type of defense the landowner may seek to assert. For the innocent purchaser and CPO defenses, in which the defendant has to show that it had no reason to know of contamination, a property owner is probably going to have a difficult time convincing a court that it had no reason to know of contamination when a consultant issues a report indicating that it needs more information to determine if there has been a release at a property. The BFPP, on the other hand, does not have to establish that it did not know or had no reason to know of contamination. Instead, a party seeking to qualify as a BFPP would be concerned about generating sufficient information from the Phase 1 so that it can comply with its post-closing continuing obligations.

The reality of the marketplace is that most lenders and real estate owners are not concerned about preserving what remain for the most part illusory CERCLA landowner liability defenses. Moreover, the vast majority of contaminated properties will not be addressed under CERCLA but under state laws. Instead, the users of the Phase 1 reports want to understand the risks associated with a particular transaction. AAI is focused on CERCLA liability and not business risk. Many lenders have developed their own environmental due diligence protocols that often exceed the ASTM E1527. These so-called ASTM-plus protocols often require consultants to examine issues not addressed by the ASTM E1527 such as asbestos, lead-based paint, lead in drinking water, radon, and mold. Likewise, users who need greater certainty are concerned about risks posed

by potential releases of hazardous substances should consider including evaluation of “business environmental risk” as an additional service.

**TO COMPLY OR NOT COMPLY? •** AAI will increase the costs and the time to complete environmental due diligence. The EPA estimated that the costs and delays would be minimal but several industry studies have indicated that the expense of performing AAI-compliant reports could increase significantly.

Many developers facing tight construction schedules and rising building costs are already implementing so-called at-risk or self-directed cleanups in which they investigate and remediate contamination encountered during construction without notifying state authorities because of concern over delays associated with reviews by understaffed environmental agencies. Purchasers and developers are not likely to incur the delays and costs associated with AAI unless they feel they are getting a significant benefit from following AAI or their lender mandates implementing AAI.

Consultants have a lot more work to do under AAI, but it is unclear how much more information the client will receive as a result of the added costs and delays. To understand the benefits of AAI, it is important to understand what it does not cover. The AAI rule does not address the following:

- What are the “reasonable steps” that all landowners must comply with after acquiring property;
- Real estate transactions that occurred before May 31, 1997. (Parties to such transactions would be required to comply with the requirements of the innocent purchaser defense. *See* 42 U.S.C. §9601(35)(B)(iv)(I));
- The CERCLA third-party defense. 42 U.S.C. §9607(b)(3);
- The CERCLA secured creditor exemption. 42 U.S.C. §9601(20)(E);

- The RCRA secured creditor exemption for USTs. 42 U.S.C. §6991b(h)(9);
- Residential real estate acquired by a non-governmental entity or non-commercial entity in which a site inspection and title search indicated there was no basis for further investigation. 42 U.S.C. §9601(35)(B)(v);
- Acquisition of title by state and local governments to properties involuntarily through tax foreclosure or by eminent domain. 42 U.S.C. §§9601(20)(D) and 9601(35)(A)(ii);
- Petroleum-contaminated sites;
- Facilities subject RCRA corrective action. 42 U.S.C. §§6924(u), (v); 42 U.S.C. §6928(h);
- Protection against claims for injunctive relief under the RCRA citizen suit provision. 42 U.S.C. §6972;
- Liability relief for cleanup of PCBs under TSCA. 15 U.S.C. §2601 et seq.; 40 C.F.R. Pt. 761;
- Persons seeking to establishing state liability defenses;
- Vapor intrusion, asbestos, lead-based paint, radon, and other indoor air quality issues.

Thus, unless the party considering AAI is a brownfield grantee, is genuinely concerned about potential CERCLA liability, or is contemplating acquiring or developing property in one of the few states that have adopted AAI as part of their state liability defenses, the burdens of AAI seem to outweigh the benefits.

To date, few lenders have revised their Phase 1 requirements to require AAI. This is not surprising because unless involved in workouts or foreclosure, they will have the benefit of the secured creditor exemption. Moreover, many banks are already using “ASTM-plus” scopes of work that require eval-

uation of issues that were not covered by E1527-00 and are not addressed by the AAI rule. Given the relatively little amount of additional information that will be generated by AAI compared with E1527-00 and the increased competition for loans, some lenders have indicated that they will continue to require ASTM E1527-00 for pre-loan diligence but will use AAI/E1527-05 before foreclosure to ensure that they will qualify for the landowner liability protections in case they lose their secured creditor exemption. Another driver for requiring AAI could be the rating agencies. However, it is also unclear if the rating agencies will require AAI for securitized loans.

Because of the pace of transactions, parties frequently triage their environmental due diligence by performing a combination of an initial ASTM E1528 transaction screen, followed by a E1527-quality investigation on problematic or more valuable properties, especially in multi-site transactions. In multi-site transactions, AAI will not be practical.

**CONCLUSION** • During the past few years, purchasers and lenders have been increasingly accepting what are commonly referred to “commodity style” environmental site assessments that have barely satisfied the AAI requirements. The significantly expanded pool of persons who can now serve as EPs virtually assures that underqualified people will issue substandard environmental site assessments. Prospective purchasers and their lenders should do more than just take the consultant’s word for it that an environmental site assessment complies with E1527: they should have their own procedures in place for verifying the information and making sure that all of the appropriate inquiries have really been made.

## PRACTICE CHECKLIST FOR The New “All Appropriate Inquiries” Rule

To take advantage of landowner liability defenses, the landowner has to show that it made all appropriate inquiries (“AAI”) with respect to the property. What this entailed was uncertain for quite some time, but the EPA has clarified the issue through the *Standards and Practices for All Appropriate Inquiries*, 70 Fed. Reg. 66,069 (November 1, 2005), which went in to effect in November of 2006.

- Key definitions of the AAI rule include the following:

— *Abandoned property*. “Abandoned property” refers to real property that can be presumed to be deserted, or when an intent to relinquish possession or control can be inferred from the general disrepair or lack of activity, such that a reasonable person could believe that there was an intent on the part of the current owner to surrender rights to the property;

— *Data gap*. A “data gap” refers to a lack of or inability to obtain information required under the AAI rule despite good faith efforts by the environmental professional or the person seeking the benefit of the landowner liability defenses. One of the more common examples is when consultants cannot trace historical use of a property back to 1940;

— *Environmental professional*. An “environmental professional” is a person who possesses sufficient specific education, training, and experience necessary to exercise professional judgment to develop opinions and conclusions regarding conditions indicative of releases or threatened releases on, at, in, or to a property.

- The components of an AAI include, among other things, the following:

— *Interviews with past and present owners, operators, and occupants*. The AAI rule requires these interviews, when necessary, to collect information on past uses and ownerships of the property and to identify potential conditions that may indicate the presence of releases or threatened releases of hazardous substances at the subject property;

— *Review of historical sources of information*. The AAI rule provides that historical sources should be reviewed back to the time that the property first contained structures or was used for residential, agricultural, commercial, industrial, or governmental purposes;

— *Searches for recorded environmental cleanup liens*. The AAI rule requires that the environmental site assessment include searches for cleanup liens that are filed or recorded against the property. Either the prospective property owner or the environmental professional may conduct the search. If the environmental professional is not instructed to conduct a cleanup lien search, the person seeking the liability protection is required to perform the lien search;

— *Reviews of federal, state, tribal, and local government records*. The AAI rule requires that the environmental site assessments include a review of federal and state government records and specifies the minimum search distance for each record. The type of records and the minimum search distances do not differ significantly from the requirements included in the ASTM E1527 standard.