

# Managing Environmental Risks in Property and Business Acquisitions: The New “All Appropriate Inquiry” Rule

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The potentials for environmental liability and environmental risk allocation issues have long been important considerations for purchasers of business assets and other property. Under the federal Comprehensive Environmental Response, Compensation and Liability Act (“CERCLA”), current owners of contaminated property are strictly liable for cleanup costs, regardless of fault or when the contamination may have occurred. Defenses to liability are few and difficult to establish. Only “innocent purchasers” who acquired property with no reason to know of the contamination could traditionally claim a defense to liability. Establishing innocent purchaser status required the property owner to prove that sufficient “environmental due diligence” was performed prior to acquiring the property to determine the absence of any actual or threatened environmental condition. The nature and extent of the due diligence required, however, was unclear and the defense narrowly construed. Historically, prospective purchasers have utilized the now-common “Phase I and Phase II” environmental site assessment process as the primary due diligence tool.

In 2002, Congress expanded the defenses to CERCLA liability available to prospective purchasers of property. Perhaps the most significant of these is the “bona fide prospective purchaser” (“BFPP”) defense. A person or entity that can establish BFPP status is not liable under CERCLA for cleanup costs as an owner of contaminated property even if that person or entity had knowledge of actual or threatened contamination prior to purchase. The threshold requirement for achieving BFPP status is performance of what is characterized as “all appropriate inquiry” (“AAI”) prior to acquiring the property.

The requirements for conducting “all appropriate inquiry” were not specifically defined in the Act. Rather, Congress instructed the U.S. Environmental Protection Agency (“EPA”) to draft regulations establishing the standards and practices to be required for satisfying AAI. In the interim, the legislation indicated that compliance with the Phase I/II standards would satisfy the AAI requirement.

On November 1, 2005, EPA issued the much-anticipated AAI rule. The new rule becomes effective November 1, 2006. Prospective purchasers and environmental professionals have nevertheless already begun implementing the requirements of the new rule in connection with business and other property transactions. As of November 2006, however, simply obtaining a traditional Phase I and/or Phase II assessment of property will not be sufficient to achieve the substantial environmental liability protections of BFPP status.

The new rule provides in detail the standards and practices required for conducting AAI. Several of the more significant changes to the current Phase I site assessment practices are as follows:

1. AAI must be conducted or supervised by an “Environmental Professional” (“EP”) who possesses specified educational, training and experience requirements described in the rule.
2. The EP will be required to review additional governmental records, consider “commonly known or reasonably ascertainable information” concerning the property and conduct more interviews of past owners and operators of the property.
3. The EP must identify and comment upon the significance of data and information gaps impacting his/her ability to identify environmental conditions potentially impacting the property.
4. The requirements for visual inspection of neighboring properties by the EP have been expanded.
5. In addition to the activities that must be performed by the EP, new requirements are placed on the prospective purchaser including searching public records for deed restrictions and environmental liens, evaluation of the prospective purchaser's own specialized knowledge of the property and assessment of the purchase price to the property's fair market in an uncontaminated condition.

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6. Under the new rule, AAI must be conducted within one year prior to the date of closing. However, many of the requirements of the rule must be conducted or updated within 180 days of the date of property acquisition.

The cost and time necessary to perform environmental due diligence will no doubt increase for most transactions under the new AAI rule and should be factored into the development of a realistic schedule for property and business acquisitions. In addition, it is likely that the standards in effect as of the date of closing will be applied. Thus, the new requirements of the new AAI rule should be considered immediately for transactions likely to close after November 1, 2006.

### **For Further Information**

Foulston Siefkin regularly counsels clients on issues relating to environmental law. If you are interested in additional information regarding this Legal Insight or if you have questions about how BFPP status and the new AAI rule may impact you, please contact **Charles Efflandt** at (316)291-9551, or email him at [cefflandt@foulston.com](mailto:cefflandt@foulston.com). The firm's diverse clientele includes private and public sector employers of all sizes, from Fortune 500 companies to small businesses and non-profit organizations. For more information on the firm, please visit our website at [www.foulston.com](http://www.foulston.com).

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