

Why You Need to Do an Environmental Due Diligence Before Buying a Property



When it comes to investing or expanding via property developments or acquisitions, environmental due diligence can save your client an unpleasant surprise (and a lot of expense), writes Kevin Cleary.



Nobody likes unpleasant surprises when buying commercial property. You – or your client – certainly don't want to lose the profit on the deal. Yet a nasty shock – and the risk of having the profit on a purchase eaten up by environmental liabilities such as unforeseen clean-up costs – is exactly the kind of gamble property buyers make when they neglect or leave it too late to do an environmental due diligence (EDD).

The practice of EDD originated in the United States in the 1970s. It's based on the principle that if land is contaminated, the owner must clean it up. Critically, though, U.S. courts have decreed that buyers or leasers of property can sometimes be on the hook for land remediation – even if it was a prior owner who caused the contamination. The news has been a cold shower for companies acquiring property and fuelled the growth of EDD as part of property transactions.

The story is slightly different in Ireland, where the EDD industry has grown out of development. Environmental regulations here are more “polluter pays” in principle, but there are legal pathways for a lender and a non-polluting owner/operator to become liable for contamination.

In Ireland EDD has tended to focus entirely on determining whether contamination has occurred. Although contaminated land evaluation is typically the main purpose, it ought not be the sole objective of EDD. A comprehensive approach to EDD should also include a more thorough assessment of many environmental aspects with associated liability concerns; for example, the operational practices of the current and historical site occupier, the presence of asbestos in buildings, the condition of the buildings, regulatory compliance with various licence or permit conditions, radon gas and impact from neighbouring sites.

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Why has EDD become important? During the industrial revolution, industry was heavily furnace-based. The waste residues from burning activities was essentially dumped and used as landfill along, for instance, the Liffey, Lee and Lagan rivers, and the inner parts of Dublin, Cork and Belfast, respectively.

Additionally, and prior to the 1990s in Ireland, it was common practice for commercial and industrial operations to bury or burn waste on-site, which included hazardous waste. With this in mind, buyers need to know the conditions of a site they're purchasing. They must price the risk of clean-up costs into their purchase price. Otherwise they're taking a shot in the dark.

Verde Environmental Consultants has come across many examples of potential money-pits in the course of completing EDD for clients on properties across Ireland. It has identified issues such as illegal waste disposal sites in Dublin, Meath and Cork, buried asbestos in Limerick, Clare and Cork, burning grounds in Mayo and Kerry, leaking underground chemical storage tanks at numerous sites across Ireland and a variety of other environmental liabilities. These liabilities can result in remediation costs ranging from €10k to over €1m, transaction delays and in some cases the collapse of the deal.

So, before your client buys a site, it needs to know what's on the site. Has the site operated in compliance with environmental regulations? What's buried underneath it? What must be done with any waste material uncovered, and how much it might cost to address a problem with contaminants?

A classic example as to when EDD is an essential part of the land or property acquisition process is where a client looks to re-develop in Dublin or on another city-centre site around the country. Say it wants to put in a car park as part of its development and space is at a premium; better then that the development includes underground basements for parking because the client is trying to squeeze in the optimum number of offices or apartments on its site.

By digging into the ground for basements, your client will likely unearth all kinds of historical waste and debris. It is legally required to dispose of that material offsite at an appropriately licenced/permitted waste facility. Some of the material may be classified as hazardous and as there are no facilities that accept hazardous industrial waste in Ireland it will need to be ferried to facilities in northern Europe. A multi-million euro bill can accrue as has been the case on numerous redevelopment sites along the Liffey. The final cost depends on the volume and composition of the soil and the site where it can be sent.

Here's how the EDD survey process works. It's typically conducted in phases, which are based on international guidelines. The EDD will include desk-based research, including analysis of geology, ground conditions under the site (trying to identify sensitive environmental receptors such as rivers, wetlands), and looking at past activities to build up a picture of historical operations on the site. Are there residential homes near the site's boundary? Who could be impacted if there is an environmental problem from this site?

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Then you do a site visit. If possible, interviews are undertaken with the facility manager or long-standing operations staff. Typically, there is also consultation with regulatory staff or the relevant local authority. What were the site's waste disposal practices? What chemicals are or were used and how are/were they stored on-site? Was asbestos used as a building material or for insulation purposes? Did they comply with their environmental permits or licences?

You need to identify if there are any fuel storage areas. Are the fuel storage tanks bunded, i.e. is there protection that if a leak happened it was contained? Is there evidence of staining on the ground? A small drip of fuel oil over 20 years can create a significant volume of contaminated soil.

It is essential that a client requiring EDD is aware of the requisite scope of work to ensure all relevant risks are assessed. Rather than falling back on the same old scope used for previous projects, the scope should be tailored to the particular transaction and facility or company being purchased. For example, asbestos should be considered for a site that will ultimately be renovated or demolished.

The risk to maintenance workers must also be considered. While an assessment of these aspects would not serve as a substitute for a comprehensive asbestos survey, it would provide a general indication of potential issues. Ignoring these aspects could result in unexpected cost and liability implications in the future.

The fallout from not doing an EDD can be significant, not to mention the cost to a client's reputation if it becomes embroiled in cleaning up a site. In 2005, for example, the Environmental Protection Agency refused to grant Roadstone approval for a legal landfill on a site the company owned in Blessington, Co Wicklow. The ruling left Roadstone with a sizeable clean-up bill, including a €25,000 annual licence charge; and a fee of €100 for disposal of each tonne of illegal waste. Over 200,000 tonnes of illegal waste were excavated. You can do the maths.

Frequently, your clients' sites will be in residential settings and so knowledge is everything. You can bury your head in the sand, ignoring issues, gambling that you'll deal with them as they arise or you can plan for challenges and understand what you're going to encounter. As the poet and orator George Herbert noted as far back as the seventeenth century: "A buyer needs a hundred eyes but a seller not one."

Timing is also critical. It's no use doing an EDD as an afterthought, as a tick-the-box exercise. It is best to do an EDD concurrently with other investigations or due diligence enquiries like, for example, a building survey or a title deeds search. If you leave it to the last minute, you lose the opportunity to use it as a key negotiating tool.

There is, after all, a silver lining to EDD. If you're armed with an EDD, which catalogues contamination on a site, it presents an opportunity for negotiation. It can be a powerful bargaining chip. It can help to get a reduction on the price of the property deal. It also presents the opportunity to walk away from the deal, knowing that you don't want this liability – that you're not willing to carry the can for historical contamination to the site.

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There is a compelling case for EDD. Without it, and failing to do it early in the purchase of a site, you're missing a trick. And you could end up costing your client a lot of undue expense.

Misconceptions about Environmental Due Diligence (EDD)

1. That you don't need to do it
 - Reality: Without an EDD, your client can be exposing themselves to a costly clean-up job.
2. That it's an expensive process
 - Reality: depending on the complexity, an EDD will cost from €2,500 to €20,000. The range in cost depends on the complexity of the site, the structure of the deal, sensitivity of location and the volume of material to be reviewed.
3. That it can delay the project
 - Reality: it won't, if it's started with enough lead-time; it typically takes two weeks to a month to conduct an EDD and it can be done alongside other property due diligence work. EDD can in fact speed up the process by identifying issues early so that they can be resolved.
4. That clients can do it at the end of the purchasing process
 - Reality: it takes time to do an EDD properly

Kevin Cleary is Operations Director of Verde Environmental Consultants Limited. For more information, visit: www.verde.ie. Verde provide EDD services to financial institutions, legal practices, as well as industrial companies.