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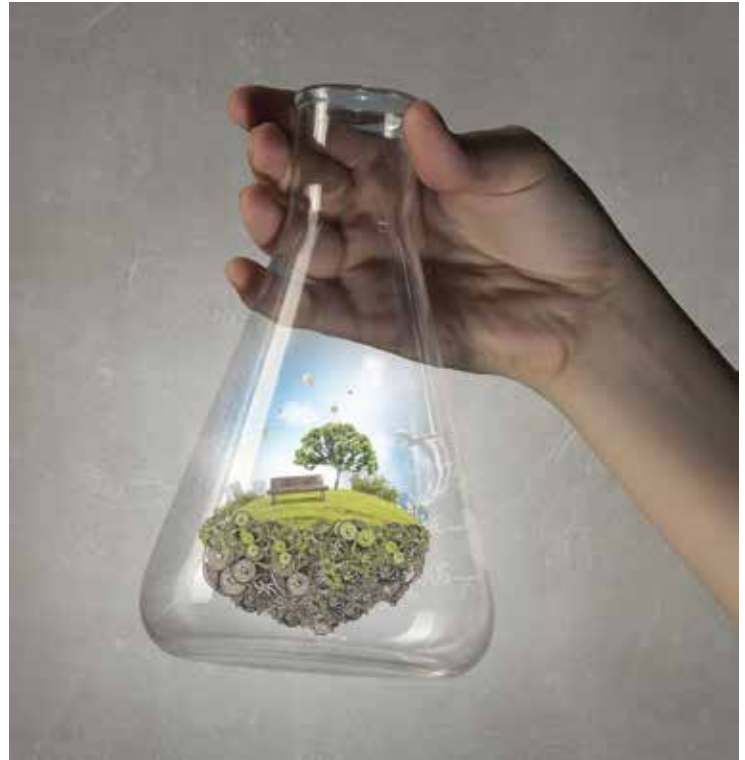
**Practical Advice
to Shift the Balance
in Your Favor**

Environmental Due Diligence

Emerging Contaminants And Changing Standards

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Environmental due diligence is a significant component of commercial real estate transactions, and a Phase I environmental site assessment (“ESA”) is the usual starting point for due diligence. Although the Phase I ESA has become a near-commodity, not all assessments are created equal, and understanding the scope of what is (and is not) encompassed by a Phase I ESA is critical to making good business decisions. Recent changes in the Phase I standard, and the increasing regulatory focus on “emerging contaminants” like PFAS and Gen X chemicals, warrant a careful review of environmental due diligence practices to ensure that risks are identified and well understood.

Updated Phase I Standard

Environmental due diligence for commercial real estate transactions, including financing, is typically based on a Phase I ESA. For many years, there was no commonly accepted standard for environmental site assessments. In 1997, the American Society for Testing and Materials (“ASTM”) first developed a standard for Phase I ESAs, and that standard has been adopted into federal and state law as the basis for various “all appropriate inquiry” defenses to liability.

In November 2021, ASTM updated the standard used for the Phase I ESA for the first time in eight years. While the revisions to the standard were numerous, the most significant updates were to clarify the definitions for recognized environmental conditions, also known as RECs. Potential purchasers (and lenders) often focus on the RECs that are identified in the Phase I ESA report, and inconsistencies and lack of clarity in the applicable definitions raised concerns about the quality and consistency of the assessments.

The updated ASTM standard, known as E1527-21, clarifies the differences between several categories of environmental concerns that may exist at a site: (i) recognized environmental conditions, known as “RECs” (unaddressed release of hazardous substances and petroleum products), (ii) historical recognized environmental conditions, known as “HRECs” (a previous release of hazardous substances or petroleum products affecting the subject property that has been addressed to the regulatory authority’s satisfaction and meeting unrestricted use criteria), and (iii) conditional recognized environmental conditions, known as “CRECs” (a recognized environmental condition addressed to the satisfaction of regulatory authorities with hazardous substances or petroleum products allowed to remain in place subject to controls). The updated ASTM standard includes a decision flow chart to accompany the updated definitions, with the goal of producing more consistent application of the relevant terminology. Additionally, the standard notes that users may wish to conduct non-scope investigations for emerging contaminants such as ‘forever chemicals,’ also known as PFAS.¹ Although these compounds are not included in the required scope of the ASTM standard, there is now heightened emphasis on the importance of these “non-scope considerations.”

Federal and state regulators are in the process of updating their regulations and guidance to reference the updated ASTM standard. Although the EPA’s All Appropriate Inquiry rule references the previous ASTM standard (E1527-13), the agency has issued a proposed rule that would allow parties to meet the All Appropriate Inquiry test by conducting a Phase I ESA pursuant to the new E1527-21 standard, or the previous E1527-13 standard. EPA set April 13, 2022 as the effective date of this new rule, in the absence of adverse comments.

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Regulatory Focus on Emerging Contaminants and 'Forever Chemicals'

State and federal regulation of emerging contaminants (also known as “forever chemicals,” “Gen-X,” and/or “PFAS”) is a significant development with the potential to impact a wide range of commercial transactions and business practices. These chemical compounds are seemingly ubiquitous, and have been found in drinking water, groundwater, wastewater, and other environmental media. Several of the PFAS compounds have been linked to adverse health effects, and recent studies have found PFAS in untreated well water in Delaware.² In addition, the average blood levels of certain PFAS compounds for residents in certain areas of Delaware are reported to be higher than national levels.³

A wide variety of PFAS compounds have been produced since the 1940's and used in a broad array of domestic and industrial applications. Uses include nonstick cookware, stain resistant coatings for carpets and fabrics, food packaging, cosmetics, shampoo, paints, and firefighting foam, among others. Once released to the environment, PFAS break down very slowly and can accumulate in humans, and the environment, hence the “forever” moniker. The useful attributes of these compounds (long-lasting, non-stick) are also the reason the compounds persist and accumulate in the environment.

Due to concerns that exposure to PFAS may lead to adverse health outcomes, regulators in many states and the EPA have increased their focus on PFAS.⁴ In Delaware, there are proposed limits on the allowable levels of certain PFAS compounds in drinking water, and these same levels will be used in the site investigation and remediation context.⁵ At a minimum, increased testing for PFAS compounds will be required, and some level of remedial efforts are likely.

Listing PFAS as Hazardous Substances

On July 2, 2018, the Delaware Department of Natural Resources and Environmental Control (“DNREC”) added PFOA and PFOS as regulated hazardous substances under the Delaware Hazardous Substances Cleanup Act⁶ and adopted the EPA's screening level of 70 parts per trillion. This policy provides that it will be in effect for three years, at which point DNREC will reevaluate the listing. DNREC has not yet issued an updated evaluation, but the agency is working with the Division of Public Health to set the drinking water maximum contaminant levels for certain PFAS compounds.

Parties involved with a Phase I ESA for commercial property located in Delaware should consider investigation of PFAS compounds as a non-scope consideration, both to evaluate potential risk and as a basis for all appropriate inquiry defenses under Delaware law. EPA has announced its intent to list PFOA and PFOS as hazardous substances under federal law, and at that point parties will need to investigate these substances to qualify for CERCLA liability protections.

When identified as part of a Phase I ESA, a suspected or actual release of PFAS will likely be considered a REC. Due to the long-lasting nature of PFAS and their ability to be present in several environmental media (soil, water, air), potential or actual PFAS contamination presents challenges for site owners, potential buyers, and lenders. Investigation and remediation of PFAS-contaminated property can be challenging because of the difficulty in accurately sampling for these compounds; PFAS compounds can be present in many fabrics and items that may contaminate samples, including in the items that store the samples themselves. Remedial technologies for PFAS contamination are still

evolving—carbon treatment of contaminated water and excavation and off-site landfilling of contaminated soil are typical remediation options, and other treatments are under development.

Importantly, the listing of PFOA and PFOS as hazardous substances in Delaware exposes previous and current property owners, operators, and other responsible parties to liability for releases of these substances. Liability for the release of hazardous substances is joint, several, retrospective, and not dependent on fault. Thus, if a buyer takes title to a property contaminated with these substances in Delaware, the buyer may be responsible to investigate and remediate these substances. Due to HSCA's strict, retroactive liability, it is possible that DNREC may require site owners and operators to investigate PFAS releases at sites that did not previously address PFAS. To protect against these outcomes, borrowers and lenders should conduct thorough diligence, and investigate the real property for potential sources of PFAS.

Enforcement and Business Risks of PFAS

PFAS manufacturers and users are now confronted with a wide range of regulatory investigations, enforcement, and litigation both in Delaware and nationally. Federal and state authorities have initiated various investigations and enforcement actions to identify past releases of PFAS, and are conducting inspections of affected sites, sending information requests, and collecting data regarding PFAS contamination. The State of Delaware recently reached a \$50 million settlement with a manufacturer of PFAS compounds regarding alleged PFAS contamination, and the funds have been deposited into a trust for assessing environmental media, funding environmental and natural resource initiatives, and financing community environmental justice and equity grants.

In addition, certain business operations may be impacted by increasing regulation of PFAS. For example, new regulations on PFAS may impact the operations of water suppliers, industrial water users, wastewater treatment facilities, and solid waste handlers. Manufacturers who use water in their operations may be impacted by the potential presence of PFAS compounds, and industries that discharge wastewater may be subject to new limits on their discharges. Disposal of solid wastes, including sludges and biosolids, is also potentially subject to new regulatory limits.

What's a Buyer (or Lender) to Do?

Parties engaged in commercial real property transactions should be aware of the recent changes to the Phase I site assessment standard, and should take steps to ensure that the appropriate ASTM standard is used by environmental professionals. In light of the focus on emerging and previously unregulated contaminants, environmental assessment and diligence practices should also be reviewed. Users and providers of Phase I ESAs should review the scope of work for environmental due diligence and site assessments to ensure that PFAS and other emerging contaminants are adequately addressed.

Standard transactional documents should be scrutinized to ensure that emerging contaminants and ongoing regulatory developments are adequately addressed. Although some commercial transactional documents now include provisions to address emerging contaminants, that is not universally the case. PFAS regulation has arrived, but parties to a commercial real estate transaction have options for diligence and risk assessment and can draft appropriate documents to allocate risk and responsibility.





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Notes:

1- "PFAS" refers to per- and polyfluoroalkyl substances. Two of the more widely used and studied PFAS chemicals are perfluorooctanoic acid ("PFOA") and perfluorooctane sulfonate ("PFOS").

2- A December 2021 report by the United States Geological Survey found PFAS to be widely distributed in untreated well water in Delaware. *See Occurrence and Distribution of PFAS in Sampled Source Water of Public Drinking-Water Supplies in the Surficial Aquifer in Delaware, 2018; PFAS and Groundwater Age-Dating Results.* (December 8, 2021), available at <https://pubs.usgs.gov/of/2021/1109/ofr20211109.pdf>.

3- In February 2022, the Centers for Disease Control and Prevention ("CDC") and the Agency for Toxic Substances and Disease Registry ("ATSDR") released a report regarding a PFAS exposure assessment of residents near the New Castle Air National Guard Base in New Castle County. The CDC assessment found that average blood levels of PFOS and PFOA in the study group were statistically higher than national levels. *See New Castle County Delaware Per- and Polyfluoroalkyl Substances (PFAS) Exposure Assessment Report.* (February 2022), available at <https://www.atsdr.cdc.gov/pfas/docs/ATSDR-PFAS-EA-Site-C-NewCastleCounty-Report-508.pdf>.

4- On October 18, 2021, EPA announced its PFAS Strategic Roadmap, which lays out the agency's regulatory strategy for addressing PFAS contamination nationwide. EPA's roadmap is centered on three strategies: increasing investment in research, implementing authority to restrict PFAS chemicals from being released into the environment, and accelerating cleanup of PFAS contamination. *See* <https://www.epa.gov/pfas/pfas-strategic-roadmap-epas-commitments-action-2021-2024>.

5- The Delaware Division of Public Health ("DPH"), which sets drinking water contaminant limits, has proposed limits of 14 parts per trillion for PFOS, and 21 parts per trillion for PFOA. DPH has issued a PFOA and PFOS Implementation Plan, which states that a proposed regulation is planned for to be issued in June 2022 and finalized in September or October 2022. *See Delaware PFOA and PFOS MCL Implementation Plan,* available at <https://www.dhss.delaware.gov/dhss/dph/hsp/files/MCLImplementationPlanPFAS.pdf>.

6- The Delaware Hazardous Substance Cleanup Act, or "HSCA," as it is known, is the Delaware state analog to the federal Comprehensive Environmental Response, Compensation, and Liability Act, or "CERCLA," also known as "Superfund." HSCA establishes the framework for remediation of contaminated sites, including Brownfields.