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The value of a phase one ESA may be better measured during bad economic times than good ones

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During the last real estate cycle where prices appeared to appreciate daily, many lenders and investors were required to move quickly. Transactions were at an all time high and competition fierce. In any industry, this kind of pressure can lead to mistakes. The environmental due diligence industry is no different. Purchaser's feeling the pressure of a back up bid for more money may have waived their right to a phase one because of the time required or accepted a lesser product such as a database only in lieu of a complete phase one. However, many of the environmental issues may go undiscovered as long as the asset is performing and the borrower is paying their bank loan on-time. In addition, during a merger between banks, many executives never look at what type of environmental report is in the folder. Did the institution being acquired require full phase one assessments on all loans or were modifications of the policy made? In addition, the amount of the loan, type of asset (multifamily vs commercial), and time frame allotted before closing play a role in why there is a subpar report or no report at all.

These days there is a more cautious approach to buying or financing commercial real estate especially when potential environmental issues such as on-site dry-cleaning operations or buried heating oil tanks arise. Lenders being the most cautious during these trying economic times and requiring phase two sub-surface assessments on a more regular basis. Since the bank's portfolios are starting to fill up with non performing loans, the last thing they need is to take back an asset with an environmental issue. If selling a loan with no environmental issues is tough these days, selling a loan with even a hint of an environmental impact can be almost impossible. If the bank suddenly realizes that there is no environmental report in the folder, what they can represent to a potential buyer is limited. That will open the door for soil and groundwater testing in order to drop the selling price even lower. To the bank this is like adding salt in a very open wound of a loan gone badly. If a bank begins a foreclosure, they may also be in need of a more comprehensive report such as the All Appropriate Inquiry (AAI). Depending on the age of the report in the file or lack of a complete phase one either an updated report or new one will help to better determine the environmental issues prior to foreclosing. These steps take time and money and the bank generally pays the fee during a foreclosure as opposed to passing it along to the borrower.

Purchasers are also taking a closer look at the potential environmental impacts than ever before. The theory of "I am getting it for a good price" does not resonate as it once did with buyer's more understanding of these costly environmental issues. A purchase price a few dollars below market can never make up for the potential cleanup cost, regulatory supervision, site disruption involved and potential law suits from tenants and neighboring property owners. Since 1994 the American Society of Testing Materials (ASTM) has provided the industry with standards on how to conduct a phase one assessment. These standards have been amended several times with the latest version being issued in 2006 as the 1527-05 standard. In 2006, Congress and the Federal Environmental Protection Agency (EPA) issued the All Appropriate Inquiry (AAI) rule which is the most comprehensive standard to date and offers purchasers some protection from cleanup liability. The rule has ten key changes from the previous standard that must be adhered to in order to qualify for the protection. The process of buying commercial property can require a lot of out of pocket expense including the legal fees, appraisal, etc..., but the phase one ESA and its value should not be overlooked. It may be the only time to understand the potential environmental impacts without the burden of the remediation lying at the feet of the purchaser or lender

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