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**SOW'S EAR TO SILK PURSE:  
COMMERCIAL REDEVELOPMENT OF  
CONTAMINATED PROPERTY**

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# **SOW'S EAR TO SILK PURSE: COMMERCIAL REDEVELOPMENT OF CONTAMINATED PROPERTY**

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The good news: Your developer client calls to tell you that he has found the perfect location for his commercial project.

The not-so-good news: The site is contaminated.

Commercial redevelopment of contaminated properties (sometimes referred to as “brownfields”) can introduce significant complexities into the project planning and construction process. Those complexities require a strategic approach to the project.

## **The Big Picture**

1. Begin with the end in mind and develop a strategy to coordinate with your plan. A critical component of the project planning process is the environmental investigation. The data developed in the investigation gives you an information baseline, so you have an idea of what you are dealing with. The scope of the investigation should be prepared with the assistance of experienced professionals (as noted in 2, below) and with the development plans in mind. Any remediation should also be coordinated with development plans. Environmental issues can be addressed using different strategic approaches. The strategic approach you and your client choose should take into account the regulatory standards, especially the cleanup targets, the project will need to meet. Above all, the approach needs to factor the client's exit plans onto the analysis.
2. Enlist the assistance of professionals with expertise and experience. Because of the complexities that can arise in development of a brownfield property, the developer is well advised to supplement, at the earliest stages of the project, the real estate/development/construction team with additional expertise. Professionals that provide that expertise will usually include an environmental attorney, environmental consultants, and remediation contractors. They may also include environmental insurance brokers and community relations and governmental affairs liaisons. The coordination between and among the different disciplines is crucial for a successful project. The team will need to closely coordinate their efforts throughout the project to address not only the “in-the-field” issues, but also legal and regulatory concerns, risk management, and governmental affairs concerns.

3. Remind your client that his risk profile regarding a deal, or the property involved, is not necessarily shared by others. You should identify fairly early in project planning other parties that will need to be satisfied with the environmental strategy chosen by your developer client and address their concerns in creating the strategy. There are numerous parties that will have a say-so regarding the developer's project (along with some others that also believe they should have input). The goals, and especially the risk profile, of those parties will not always match up with the developer's. Those parties may include:

- governmental agencies (multiple federal, state and local)
- equity investors
- lenders
- insurers
- future tenants
- future purchasers
- community "stakeholders"

Do not automatically assume that if your client is willing to take the risks, there will be another party in the future that will provide an exit strategy by buying or leasing the project. I have seen developers caught in the so-called "risk sandwich." They have decided to purchase a brownfield site, but because of the environmental issues presented, equity investors and lenders do not want to get involved, and the developer is not able to proceed with the deal.

4. Recognize the issues of concern to the various parties. One of my former partners used to say that all deal makers are motivated and constrained by a balance between greed and fear. Brownfield deals are no different. But, there are some other factors that your client and other parties will focus on and that you should consider in providing advice, including the following:

- enhanced liability exposure
- lack of certainty and finality
- cost
- timing
- complexity
- acceptability of cleanup standards
- access to financing
- access to insurance

5. Never lose sight of the fact that you are working on a real estate project. Although environmental issues may impact a project on multiple levels, do not let other parties turn it into a science project. You need to use environmental consultants that understand your client's business goals and can serve as advocates to further those goals, rather than just acquiescing in the government's usual requests for more detailed data. Also, while there are various "tools" (summarized in Section II of Addendum A) to address environmental issues, solving the problems can involve

extra cost and additional time, both of which may be significant. The strategy used should be re-evaluated at various states of the project. At the end of the day, the redevelopment potential and deal economies have to make sense before the developer proceeds with the project.

## The Details

Noted below are various strategic and practical considerations that arise in the planning and construction phases of a project where contaminated property is being redeveloped.

### A. Media Specific Concerns

- Soil
  - Shorter-term remediation
  - Soil management of known impacted materials
- Groundwater
  - Longer-term remediation
  - Management of groundwater encountered

### B. Remediation Strategies

- Layered remediation: soil first, then groundwater
- Staged remediation: remediate, then build
- Engineering controls: cap, then build
- Integrated remediation: coordinating site remediation with development
- UST closure only

### C. Addressing Site Soils

- Testing considerations
  - Imported fill
  - Exported fill
- Grading plan and balancing determinations
- Feasibility of coordinating geotechnical and environmental soil investigations

### D. Addressing Specific Regulated Matters

- Demolition
  - Asbestos
  - Lead Paint
  - Other materials
- Waters of the United States
- Methane/vapor issues

E. Protecting Designated Areas

- Monitoring wells
- Areas of known contamination (cross-contamination concerns)

F. Managing Other Issues

- Clean-up target levels
- Impact of controls on proposed redevelopment
  - Deed restrictions and other institutional controls
  - Engineering controls
- Other regulatory issues
  - Regulatory decision process
  - Reopening a previously closed site
  - Storm water regulations
  - Dredge and fill permits
  - Worker safety concerns
- Multiple overlapping governmental jurisdictions
- Unexpected site surprises

**Other Matters**

There are a myriad of issues that should be considered in crafting an effective strategy for commercial redevelopment of contaminated property. Formulating that strategy will require not only the multi-disciplinary approach noted above, but also what one of my clients referred to as a “multidimensional analysis”.

Addendum A is provided as a checklist of environmental legal issues to be considered in the pre-purchase stage of a potential project. Addendum B is another overview that identifies various issues relating to the purchase, redevelopment, and operation phases of a project.

## **A BUYER'S CHECKLIST OF ENVIRONMENTAL LEGAL ISSUES**

The following checklist notes environmental legal issues to be considered by a buyer looking at redevelopment of contaminated property. The checklist does not purport to be all-inclusive, in part because brownfield issues are so site specific.

### **XXI. Loss Exposures**

- A. Liability Exposure**
  - 1. Potential Liabilities
    - a. Remediation
    - b. Property damage
    - c. Personal injury
    - d. Natural resource damage
    - e. Post-closure obligations
    - f. Fines and penalties
    - g. Injunctive relief
    - h. Stigma damages
    - i. Contractual obligations
    - j. Covenants running with the land
    - k. Successor liability
  - 2. Potential Complainants/Plaintiffs
    - a. State government
    - b. Federal government
    - c. Local government
    - d. Onsite persons
    - e. Offsite persons
    - f. Contract beneficiaries
  - 3. Notification Obligations
    - a. Release reporting
    - b. Disclosure
- B. Other Exposures**
  - 1. Increased construction and development costs
  - 2. Potential cleanup cost overruns
  - 3. Increased operating expenses
  - 4. Increased costs of financing
  - 5. Business interruption/construction delay
  - 6. Restrictions on use
  - 7. Impaired future marketability and resale value

## XXII. Tools for Managing Exposures

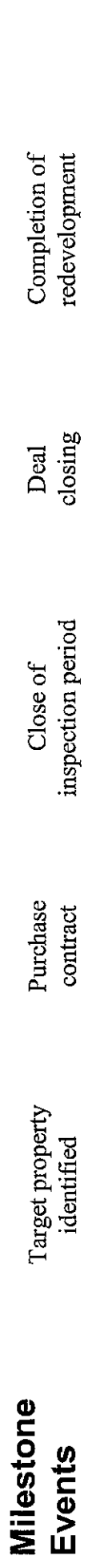
- A. Older Tools
  - 1. Environmental assessment/due diligence
  - 2. Contractual risk allotment mechanisms
  - 3. Price reduction
  - 4. Seller post-sale remediation agreement
  - 5. Cost recovery/contribution
  - 6. Assignment of claims
  - 7. Carve out of portions of tract
  
- B. Newer Tools
  - 1. Risk-based cleanup programs
  - 2. Protection from liability to government
    - a. State Voluntary Cleanup Programs (VCP)
      - (1) Liability releases for new owners and lenders
      - (2) Enforcement bar
      - (3) "Conditional" certificates of completion
    - b. Texas Innocent Owner/Operator Program (IOP)
    - c. Texas Dry Cleaner Remediation Statute
    - d. New/revised CERCLA liability exemptions and defenses
      - (1) Contiguous Property Exemption & Pre-certification
      - (2) Bona Fide Prospective Purchaser Defense
      - (3) Innocent Landowner Defense
    - e. EPA Ready for Reuse Initiative
    - f. EPA Prepurchase Agreements
    - g. EPA Memoranda of Agreement
    - h. EPA Policy Regarding Groundwater Contamination from Offsite Sources
    - i. EPA NFRAP Designation
  - 3. Municipal Setting Designation (Texas) / urban setting designation (elsewhere)
  - 4. Lender liability protections
  - 5. Government reimbursement funds
  - 6. Liability transfer programs
  - 7. Environmental insurance
  - 8. Tax incentives
  - 9. Economic incentives

## XXIII. Structuring Considerations

- A. Entity Selection
- B. Form of Transaction
- C. Tax Considerations
- D. Post-Acquisition vs. Pre-Acquisition Remediation

# Addendum B

## Environmental Issues in Real Estate Purchase, Redevelopment, and Operations



Milestone Events	M-1 Target property identified	M-2 Purchase contract	M-3 Close of inspection period	M-4 Deal closing	M-5 Completion of redevelopment	
Phases of Activity	P-1 Property Search	P-2 Negotiations	P-3 Due Diligence	P-4 Financing & Pre-Closing Activities	P-5 Site Redevelopment	P-6 Site Operations
<b>Environmental Activities</b>	↑	↑	↑	↑	↑	↑
<b>Identify and Evaluate Risks</b>	<ul style="list-style-type: none"> <li>Environmental site screening</li> </ul>	<ul style="list-style-type: none"> <li>Seller disclosures and representations</li> <li>Inspection and access rights</li> </ul>	<ul style="list-style-type: none"> <li>Environmental site assessment</li> <li>Legal analysis</li> <li>Financial analysis</li> </ul>	<ul style="list-style-type: none"> <li>Lender due diligence review</li> <li>Loan default provisions</li> </ul>	<ul style="list-style-type: none"> <li>Demo/construction risk assessment (site strategy, controls, regulated activities, safety)</li> </ul>	<ul style="list-style-type: none"> <li>Self-audits</li> <li>Tenant/supplier audits and contract review</li> </ul>
<b>Manage Risks</b>	<ul style="list-style-type: none"> <li>Contract termination rights</li> <li>Duty to address pre-existing conditions</li> <li>Cleanup standards &amp; controls</li> </ul>	<ul style="list-style-type: none"> <li>Consultant selection</li> <li>Professional services agreement</li> <li>Privilege and confidentiality</li> <li>Notice &amp; reporting</li> </ul>	<ul style="list-style-type: none"> <li>Pre-closing remedial action</li> <li>VCP / IOP co-application</li> <li>Pre-purchase agreements with government</li> </ul>	<ul style="list-style-type: none"> <li>Pre-closing remedial action</li> <li>VCP / IOP co-application</li> <li>Pre-purchase agreements with government</li> </ul>	<ul style="list-style-type: none"> <li>CERCLA due care</li> <li>Voluntary cleanup</li> <li>Asbestos and mold abatement</li> <li>Construction &amp; soil management</li> </ul>	<ul style="list-style-type: none"> <li>Permitting</li> <li>Compliance and reporting</li> <li>Lease terms &amp; tenant oversight</li> <li>Env. mgt. systems</li> </ul>
<b>Finance Risks</b>	<ul style="list-style-type: none"> <li>Remedies &amp; risk allocation</li> <li>Purchase price</li> <li>Financial assurance</li> <li>Assignment of claims</li> </ul>	<ul style="list-style-type: none"> <li>Consultant insurance</li> <li>Third-party claims analysis</li> <li>Brownfield financial and tax incentives</li> </ul>	<ul style="list-style-type: none"> <li>Insurance selection, application and underwriting</li> <li>Escrows and other financial assurance mechanisms</li> </ul>	<ul style="list-style-type: none"> <li>Insurance selection, application and underwriting</li> <li>Escrows and other financial assurance mechanisms</li> </ul>	<ul style="list-style-type: none"> <li>Cost cap insurance</li> <li>Fixed cost cleanup contracts</li> <li>PLL insurance (excl. known conditions)</li> <li>Contractor insurance</li> </ul>	<ul style="list-style-type: none"> <li>Self-retention</li> <li>Indemnification</li> <li>PLL insurance</li> <li>Litigation</li> </ul>

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