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Who is the Environmental Consultant Working For?©

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A recent California case (*Mao v. PIERS Environmental Services, Inc.*, No. H041214, Cal: Court of Appeal, 6th Appellate Dist. 2017) serves as a reminder of why it is important for the parties to a transaction to understand their relationship with the environmental consultant performing a site investigation, as well as the purpose of that investigation. In the *Mao* case, a California appellate court held that an environmental consultant hired by a lender had no duty to a prospective purchaser of contaminated property. The environmental consultant had prepared a report that indicated no site contamination at property for which the bank was extending a secured loan. The borrower purchased the property and in connection with later investigation, petroleum contamination was discovered.

Prospective purchasers, in particular, should look beyond the conclusions of a consultant's environmental site assessment or investigation report and determine what recourse they may have if the consultant has missed in its entirety, or mischaracterized, material information regarding the site being assessed. If a party other than the purchaser, including an affiliate of the purchaser, has commissioned the report, the purchaser will not be in contractual privity with the consultant and could not then bring a breach of contract action. Purchasers typically work around this barrier by having the consultant confirm that the purchaser can rely on the report. That is typically done through a reliance letter. In the reliance letter, the consultant will allow the purchaser to rely on the report to the same extent as the party to whom the report was addressed.

A consultant's engagement agreement with its client typically provides, among other things, for a limitation of liability and establishes a standard of care. The liability limit is usually a very low number, especially with respect to a Phase I ESA where a competitive marketplace keeps the cost that can be charged for a report low. Many times the consultant's liability limit is tied to the lower of the Phase I ESA cost and a set amount, like $5,000. Unless the party that engaged the consultant negotiated a higher liability exposure, the damages suffered from a defective consultant's report will significantly exceed the available monetary remedy established by the consultant. The standard of care established in the consultant's engagement is typically

stated as being in accordance with generally accepted engineering and environmental consulting principles and practices, and consistent with that level of care and skill ordinarily exercised by other professional consultants under similar circumstances at the time the services are performed. That is not a particularly high bar for the consultant to clear. Also, many times there will be language in the consultant's report that attempts to set further limitations or qualification on the standard of care.

In the California case, the purchaser argued that the consultant owed it a duty even though the purchaser was not a party to the contract. The court rejected that position. It considered that the primary objective of the assessment was to inform the lender's due diligence in connection with a financial transaction and that any intent to protect the prospective buyer was at best secondary. The court's focus on the lender's due diligence needs also points to why the potential buyer may not want to depend on the scope of assessment used by a lender. Lenders enjoy certain liability protections from strict, joint and several environmental liability under federal and state environmental laws, which purchasers do not enjoy. The "secured creditor exemption" will allow lenders to avoid environmental remediation liability for property in which they have security interest if they do not participate in management of the property prior to foreclosure and, following foreclosure, if they take commercially reasonable steps to divest themselves of ownership. Even where lenders will require an ASTM E1527-13 Phase I environmental report, the scope of that report will not cover environmental concerns of interest to certain purchasers. For example, that report form does not address asbestos, lead-based paint or mold issues, which will be of interest to borrowers planning to refurbish buildings, or wetlands and endangered species issues, which will be of interest to borrowers planning to redevelop the property.

Consequently, a prospective purchaser is well advised to obtain reliance from consultants performing environmental investigations for third parties or affiliates of the prospective purchaser, and to consider whether an environmental consultant's report commissioned by another party will meet the needs of the prospective purchaser even where reliance is available.

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