Chapter 1
Transaction Documents

PART ONE:

CONSIDERATIONS IN DRAFTING TRANSACTION DOCUMENTS

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TRANSACTION DOCUMENTS

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I. Introduction

Transactions involving the sale of real property and other assets are memorialized in documents intended to reflect the parties' intentions. These documents, such as agreements of sale, are typically prepared by counsel. Sophisticated sellers of contaminated properties often engage counsel early in the process to provide advice on the numerous issues pertaining to contaminated properties. Buyer's counsel, on the other hand, is often not retained until the client has already reached some preliminary decision to buy the property. Seller and buyer have different perspectives. The seller is looking to dispose of a parcel of land and retain little if any post-closing obligations or liabilities. Buyer is looking to acquire property, often for a specific purpose, and acquire as little liability for environmental problems as possible. Counsel for both parties will be asked to provide advice regarding the conditions of sale from an environmental perspective.

Putting together a successful deal, i.e. getting the parties to yes, or even to "no thank you," is a function of numerous interrelated considerations. The nature of the risk is paramount, including whether it is capable of being addressed and allocated. The parties must consider whether the risk would involve an interface with government agencies, in particular the Pennsylvania Department of Environmental Protection (DEP). If so, the parties will need to ascertain how to resolve issues relating to that government interface. A significant issue involves which of the two parties is willing to bear the risk of contamination. Often, the answer to that question comes down to which of the two parties wants the deal more.

Should the two parties come to an understanding, drafting the transaction documents to reflect the resolution of the various issues is the lawyer's task. This discussion will highlight several issues, but is by no means an exhaustive review of all of the various permutations and complicated scenarios that practitioners encounter.

II. The Seller's Perspective

Discussions often begin with the buyer's perspective, in part because due diligence inquiries focus on the buyer. Yet any potential transaction begins with a person willing to sell the property.

The level of knowledge and preparation of a seller is wide ranging. Consider the seller of commercial real estate on whose property exists several buildings which may contain asbestos containing materials, gasoline service stations and dry cleaning establishments. In the absence of a documented release, those commercial owners have little interest in allowing the significant pre-agreement due diligence inquiry into environmental risks present on the property. In many instances, those sellers have a valuable piece of commercial real estate in an area of prime development opportunities who may be unwilling to be flexible on purchase price, may be unwilling to give any representations and warranties regarding the condition of the property and will require strict adherence to timeframes.

Also consider the owner of a gasoline service station and the real estate on which it is situated, who is well aware that leaks have likely occurred over the station's life of operations resulting in some level of contamination of the ground. Again, in the absence of any documented releases, that seller may be unwilling to allow invasive environmental testing of the property and may even insist on an "as is-where is" transaction where the buyer accepts the risk of existing contamination.

Another example is the seller of an industrial complex on which heavily regulated industrial activities have occurred under permits issued by DEP. Those properties may have been the subject of investigation and enforcement action, and even some remedial action. The seller would prefer that the buyer rely upon those investigations and not conduct any additional invasive testing for fear of the discovery of additional areas of previously unknown contamination or the discovery of new types of contaminants.

In many instances, the seller will find itself in a position where it must either allow the buyer to conduct a level of due diligence investigation necessary to satisfy recent standards, or take the property off the market. Even if the seller is not willing to allow invasive testing, it must be prepared to disclose all documents relating to environmental conditions of the property and knowledge of environmental risks. In most instances, a buyer will insist upon a representation and warranty that the seller is unaware of the presence of hazardous wastes and/or hazardous substances on the property and/or is unaware of the existence of any conditions that might give rise to a requirement to remediate the property under applicable environmental laws. In light of USEPA's final regulation defining the term "all appropriate inquiry" (70 Fed. Reg. 66070 (2005)) and ASTM's Standard 1527-05 for conducting Phase I Environmental Site Assessments, sellers often will need to be prepared to respond to intensive questioning, detailed reviews of government records and a greater tendency for environmental consultants to recommend invasive testing as part of a Phase II inquiry.

III. Buyer's Perspective

Like sellers, buyers come in all shapes and sizes. There is the large sophisticated commercial or corporate buyer seeking to acquire a location for expanding facilities that is savvy on environmental issues and has several options for relocation or expansion, thereby giving it

some leverage over sellers. There are speculative buyers, knowledgeable about environmental risks and tools to manage those risks (such as insurance options), who are seeking to acquire and flip properties in areas of future potential development and may have some greater level of tolerance for environmental risks. Then there is the buyer who has identified a piece of property on which a business currently exists that would enhance the buyer's current business, for example, a heating oil distributor who is seeking to acquire smaller competitors with small bulk plants in rural areas. This buyer is knowledgeable of the risks and operations, and its priority is to acquire.

Buyers may be concerned about potential liability under a variety of federal and state statutes, including, but not limited to the Comprehensive Environmental Response Compensation and Liability Act ("CERCLA"), Pennsylvania's Hazardous Sites Cleanup Act ("HSCA"), the Pennsylvania Storage Tank Spill Prevention Act ("STSPA"), the Pennsylvania Clean Streams Law and the Pennsylvania Solid Waste Management Act, among others.

Potential liability under CERCLA can potentially be avoided by an innocent purchaser who establishes that they are a "bona fide prospective purchaser." To establish this defense, the purchaser must show that:

- All disposal occurred prior to the acquisition of the property;
- The purchaser conducted "all appropriate inquiry" prior to closing on the property;
- The purchaser provided all legally required notices regarding the discovery of release of hazardous substances;

- It undertook "Appropriate care" by taking reasonable steps to stop any continuing release, prevent threatened future releases, and prevent or limit exposure to previously released hazardous substances;
- The purchaser cooperated and provided access to any person or the government responsible for conducting any future cleanup; and
- The purchaser abided by and did not interfere with any institutional controls or land use restrictions imposed upon the property.

40 U.S.C. § 9601(40) and 9607(r).

EPA's new rule defining "all appropriate inquiry" (70 Fed. Reg. 66070 (2005)), effective November 1, 2006, further clarifies the agency's view of what constitutes "all appropriate inquiry." ASTM's standard 1527-05 conformed to EPA's rule. A buyer must consider compliance with EPA's rule to enhance the prospect of being considered a bona fide prospective purchaser. In some situations, an approach more tailored to this specific situation may justify mixing and matching from different due diligence techniques.

One must remember that the defense to CERCLA liability does not necessarily provide a defense to the state statutory schemes referenced above. Indeed, following the CERCLA all appropriate inquiry checklist may not necessarily be appropriate where only petroleum-derived contamination is involved. Engaging in environmental due diligence serves other useful purposes, including:

- Developing a baseline of environmental conditions which may be necessary with respect to indemnities.
- Identifying for the buyer various compliance issues which it may need to address if it intends to continue running a business. Information regarding environmental

compliance and permitting during the due diligence process is essential for a buyer intending to continue an existing business to understand dates for permit transfers, compliance reporting and other regulatory obligations.

- Obligations required in physical changes to be made to the property and structures thereon, including requirements for asbestos removal prior to excavation, risks involved in significant excavation and exposure considerations with respect to changes in use from industrial to mixed use and/or residential applications.
- Developing a comprehensive understanding of the environmental conditions of the property to the extent relevant to adjustment in the purchase price.

IV. Transaction Documents

The transaction for the sale of property with environmental risks can involve the use of several documents. These documents serve different purposes, and memorialize the intentions and agreements of the parties to the transaction.

A. Letters of Intent

Letters of intent can be used by the parties as an expression of their intent to enter into an agreement for the sale of real estate. The letter of intent typically will define the property to be purchased, specify the purchase price, and detail the conditions under which Buyer will be obligated to purchase, such as seller's satisfaction with certain obligations and buyer's satisfaction with non-invasive investigations. It is important to note that a letter of intent is not legally binding on the parties unless it expressly so states. Indeed, letters of intent usually expressly provide that they are not legally binding on either party.

Letters of intent can be of use when a willing buyer is interested in the property yet needs some time to evaluate further whether the property will suit its needs regarding zoning and other

restrictions. It may also be useful on Act 2 sites where the buyer intends to put the property to an industrial use and needs some time to investigate and wants the seller to agree not to market the property for a limited period of time. As consideration for removing the parcel from the market, the seller typically will want hand money which is forfeited to seller in the event an agreement of sale ultimately is not executed. It is often the case, however, that a seller will be unwilling to remove the property from the market and instead presses the buyer to generate a sales agreement the parties can sign. A copy of a draft Letter of Intent is attached for reference. In that instance, the Seller had several obligations under a Consent Agreement with DEP relating to an Act 2 site that remained unsatisfied, yet was close to full compliance. The sale was dependent upon seller's satisfaction of those obligations so buyer would not assume such obligations and would instead gain full Act 2 liability protection.

B. Access Agreements

Provisions regarding access are often built into the agreement of sale. In some instances, provisions for access can be included in stand alone agreements. In both instances, there are several considerations that are often included in access agreements.

1. Scope – The seller may give the buyer free reign. On the other hand, the seller may demand a specific scope of work, identifying locations to be sampled and contaminants to be analyzed.
2. Duration – The buyer will want to confine access to certain times of the day, typically during reasonable business hours, in a manner that does not interfere with seller's use of the property.
3. Access to records and employees – If the buyer seeks access to the seller's records, and the seller is a business, confidentiality provisions should be

included to protect sensitive business information. If access to employees for interviews is sought, language should be included to address the conditions of such access.

4. Indemnity – Seller will typically insist on a clause by which buyer agrees to hold harmless, defend and indemnify seller from and against any and all damages, claims, causes of action, actions and liability arising from buyer's activities relating to access.

5. Insurance – Seller should request proof of insurance from all consultants and other entities that will access the property. Seller may want to be named an additional insured on those policies.

C. The Agreement of Sale

The agreement of sale memorializes the parties' intentions regarding every aspect of the sale. Since they typically include integration clauses, the agreement must accurately reflect the meeting of the parties' minds on each topic. The following is a list of the topics typically addressed in the agreement of sale, with a brief discussion of issues.

1. Description of the real property being purchased. While this topic seems straightforward, it is important not only for the parties to include an accurate description of the land, but also all fixtures (considered part of the real estate) and other structures that are the subject of the sale.

2. Description of any personalty and other assets being conveyed. Purchases may include manufacturing or process equipment which must be separately listed as assets which are being conveyed. For example, sales of fuel dispensing locations should include a specific list of all tanks, lines,

dispensers, pumps, leak detection equipment and all other equipment being conveyed. If the sale is to include customer lists and information, those items should be listed as well. Records of the business pertaining to the assets being acquired, such as records regarding purchases and maintenance of equipment, fees paid to governmental agencies, permits and other documents pertaining to compliance with regulatory compliance should be specifically listed.

3. The Title to be conveyed. A buyer will want title to be free and clear of any and all liens and encumbrances conveyed by general warranty deed. Contaminated properties, including Act 2 sites, are often conveyed by special warranty deed due to the requirements for placement in the deed of notices of the disposal of hazardous substances under the Hazardous Sites Cleanup Act, 35 P.S. § 6020.512(b) and/or hazardous wastes pursuant to the Solid Waste Management Act, 35 P.S. § 6018.405.

4. Expression of Purchase Price. The parties often want to allocate the purchase price among the land, equipment and customer lists. If the property is contaminated, the parties may allocate a smaller portion to the land. In some instances, the parties want to include a clause providing for adjustment of the purchase price in the event certain contingencies arise. However, if the buyer has the option to terminate the agreement based upon information developed during the period of due diligence, there is no reason the parties cannot renegotiate the price and enter into a modification to the agreement of sale.

5. Commitment for Title Insurance. Buyers often desire title insurance. The title insurer will review title and will identify exceptions. Environmental

conditions may present an exception, for example if title is already clouded with a HSCA notice of the release of hazardous substances. The title insurer will issue a report containing a list of unpermitted exceptions. The agreement should provide that in such an event, the buyer notifies seller thereof and seller has a defined period of time to cure those exceptions by correcting them or committing to insure over them. The agreement should further provide that if seller is unable to cure those exceptions within the defined period, then buyer has the option to either terminate the agreement or proceed with the sale and accept title subject to the unpermitted exceptions not corrected.

6. The Due Diligence Period. It is fairly routine now for buyers to insist on a period of due diligence during which buyer has the opportunity to investigate the property to identify the risks of ownership, including contamination. Due diligence provisions address the following issues.

   a. The right to inspection and access. Provisions address the conditions under which the buyer is given the right to inspect the property and access to records and employees. The same considerations addressed above with respect to stand alone access agreements apply. Note that in some instances, the seller may refuse to permit invasive testing. If so, the practitioner should consider whether to include language indicating that invasive testing is not being allowed. It is unclear whether such a clause would provide the buyer with any protection if it proceeds nonetheless with the sale.

b. Reliance of buyer on inspection only. Where buyer is given the right to inspect, seller may insist on a clause stating that buyer is relying solely on its examination of the property and not on any information supplied by seller. Such a provision may also state that upon closing, buyer waives any right or claim against seller relating to the condition of the property except as to express representations and warranties.

c. Results of the due diligence period. The parties should define the consequences of buyer's due diligence. Agreements may include a provision under which a buyer dissatisfied with the condition of the property based on its investigation has the right to terminate the agreement a within a specified period of time, typically the last day of the due diligence period. Seller will want a provision stating that the buyer must provide written notice of termination by that date, and if no such notice is received, then buyer waives all objections to the environmental condition of the property. Standard form realtor agreements for commercial properties now contain such clauses.

7. The condition of the property – "as is, where is" clauses. Sometimes, a seller will insist that the property be sold "as is, where is, with all faults." Under Pennsylvania law, this language precludes the buyer from suing seller for breach of contract or warranty. Juniata Valley Bank v. Martin Oil Co., 736 A.2d 650 (Pa. Super. 1997). Such language will not serve to allocate or eliminate liability under environmental statutes. M&M Realty Co. v. Eberton Terminal Corp., 977 F.Supp.683 (M.D. Pa. 1997). Rather, express language

clearly manifesting the parties' intent to transfer such statutory liability is required. Id.

8. Representations and Warranties.

As noted earlier, each party to the transaction will have a different perspective with respect to representations and warranties, particularly regarding environmental matters. There are several areas that should be addressed with respect to representations and warranties from an environmental prospective. One of the first things the parties should do is define their terms.

a. Defining the Terms. The language used with respect to environmental representations and warranties is critical. There are different terms that could be selected and ways to define those terms. By defining the terms "environment", "environmental laws", "facilities," "hazardous materials" and "release," the agreement can provide the parties with a basis to address representations and warranties.

i) "Environment" means soil, land surface or subsurface strata, surface waters, groundwaters, drinking water supply, air, plant and animal life, and any other environmental medium or natural resource.

ii) "Environmental Laws" means any Legal Requirement pertaining to the protection of the Environment, which govern:

(a) the existence, clean-up, remediation and/or removal of contamination from property;

(b) the emission or discharge of Hazardous Materials into the Environment;

(c) the use, generation, transport, treatment, storage, disposal, removal, or recovery of Hazardous Materials; or

(d) any other actions designed to protect public health and the Environment.

iii) "Facilities" means any real property, leaseholds, or other interests owned or operated by Seller and any buildings, plants, or structures owned or operated by Seller.

iv) "Hazardous Materials" means any waste or other substance that is listed, defined, designated, or classified as, or otherwise determined to be hazardous, radioactive, or toxic or a pollutant or a contaminant under or pursuant to any Environmental Law, including any mixture or solution thereof, and specifically including petroleum and all derivatives thereof or synthetic substitutes therefore and asbestos or asbestos-containing materials and, even if not so listed, defined, designated, classified or otherwise determined, such term shall also include any waste or other substance that is, or may be, harmful to any Person or the Environment.

v) "Release" means any spilling, leaking, pumping, pouring, emitting, emptying, placing, discharging, injecting, escaping, leaching, dumping, or disposing, into the Environment, whether intentional or unintentional.

b. The representations and warranties then follow on these definitions. As would be expected, the seller will want narrowly tailored representations

and warranties. The seller typically will only want representations to be based on actual knowledge rather than providing absolute warranties regarding the presences of hazardous materials. The buyer will want the representations to be as broad as possible, especially with respect to the seller's operations and compliance with law. Note that in order for a buyer to prove a breach of an actual knowledge representation, it must prove that the seller was aware of the condition and made a false statement.

i) Representations regarding compliance with law.

(a) Except as set forth in [a schedule], Seller is in compliance with and has not been and is not in violation of or liable under, any Environmental Law, except for such failures to comply or violations of which would not reasonably be expected have a Material Adverse Effect. Seller has not received any actual or threatened order, notice, or other communication from (i) any Governmental Body or private citizen acting in the public interest, or (ii) the current or prior owner or operator of any Facilities, of any actual or potential violation or failure to comply with any Environmental Law.

(b) To seller's knowledge, the Property complies with all applicable Environmental Law, and, to seller's knowledge, all requisite permits necessary to own, operate, maintain and use the Property in compliance with such legal requirements, as the Property is

currently being used by seller as of the date of this Agreement, have been issued and are in full force and effect.

ii) Representations regarding pending claims Except as set forth in [schedule], there are no pending or, to the Knowledge of Seller, Threatened claims, Encumbrances, or other restrictions of any nature arising under or pursuant to any Environmental Law, with respect to or affecting any of the Facilities.

iii) Representations regarding violations of environmental law. Except as set forth in [schedule], Seller has not received any citation, directive, inquiry, notice, Order, summons, warning, or other communication, written or oral, that relates to Hazardous Materials, or any alleged, actual, or potential violation or failure to comply with any Environmental Law with respect to any of the Facilities or with respect to any property or facility to which Hazardous Materials generated, manufactured, refined, transferred, imported, used, or processed by Seller or any other Person for whose conduct they are not or may be held responsible, have been transported, treated, stored, handled, transferred, disposed, recycled, or received.

iv) Representation regarding the use, presence and handling of Hazardous Materials. Except for Hazardous Materials that are reasonably necessary to operate the business of Seller in the Ordinary Course of Business, which are listed on [schedule], there are no Hazardous Materials present on or in the Environment at the Facilities, and all

such Hazardous Materials are stored and handled in accordance with all applicable Environmental Laws.

v) Representations regarding the release of Hazardous Materials.

(a) Except as set forth in [schedule], there has been no Release of any Hazardous Materials or, to the Knowledge of Seller, immediate threat of Release at or from the Facilities or at any other locations where any Hazardous Materials were generated, manufactured, refined, transferred, produced, imported, used, or processed from or by the Facilities.

(b) Seller is not aware of any Release or threat of release of any Hazardous Materials from the Facilities or at any other locations on the Property.

vi) Representations regarding the presence of underground storage tanks. Seller is not aware of the presence of underground storage tanks on the Property other than those specifically listed on Exhibit A.

vii) Representations regarding the delivery of all environmental reports. Seller has delivered, or has caused to be delivered, to Buyer a copy of all reports and studies that have been prepared by environmental or engineering consultants which are in the possession or control of Seller or its agents or representatives including, but not limited to, such reports and studies as may be held by any attorney or by Sellers pursuant to any attorney-client privilege, pertaining to the presence or suspected presence of Hazardous Materials in, on or under the

Facilities, or concerning compliance by the Seller, or any other Person for whose conduct they are or may be held responsible with Environmental Law.

D. Closing Deliverables.

There are several documents that may be necessary to convey "title" to the acquired assets at the closing of a transaction.

1. The deed – It is important that the deed accurately reflect any restrictions relating to environmental issues. For example, if deed acknowledgements are required under HSCA or SWMA, they must be included and properly worded. References to use restrictions and institutional controls applicable to Act 2 sites or properties otherwise subject to such encumbrances must be clear and accurate. The language for use restrictions and institutional controls relating to properties at which DEP has involvement should follow the language DEP has found acceptable. With respect to properties that have proceeded through the Act 2 process, the language should track that which was already approved by DEP in that process.

2. Bill of sale – The bill of sale should list all of the items of personalty that are part of the transaction, including equipment, tanks, vessels, corporate records and all other items being sold that are not real estate.

3. Irrevocable assignment – Whenever the buyer is purchasing an ongoing business or a customer list, an irrevocable assignment should be used to ensure that all rights of the seller in and to such tangible and intangible assets are conveyed to buyer.

V. Using Buyer-Seller Agreements and Prospective Purchaser Agreements in Transactions.

In the Act 2 program, the Buyer-Seller agreement is used to foster the purchase and reuse of contaminated sites by innocent entities by providing certainty with respect to the purchaser's obligations regarding the condition of the property. A prospective purchaser may be interested in developing the property, but doesn't want the uncertainty of exposure to open-ended liability for site contamination it did not cause. Buyer-Seller agreements have also been used to further the purchase, remediation and reuse of properties contaminated as a result of releases from underground and aboveground storage tanks that contained petroleum products. Further, DEP has the authority under the Hazardous Sites Cleanup Act to covenant not to sue "innocent" purchasers of HSCA sites, which is formalized in a Prospective Purchaser Agreement. In each of these instances, the purchaser and its affiliates must not have caused or contributed to the contamination of the site.

These buyer-seller documents are now fairly well known to sophisticated entities in the real estate industry. They can be used by a seller of contaminated property in the context of a transaction in which the only way the property can be sold is if the prospective purchaser gets liability protection. For example, consider the owner of a parcel of land on which a gasoline service station was operated. The owner leased the property to the gas station's owner, who went out of business in the 1990's. The property owner had no involvement in the business. A prospective purchaser seeking to redevelop the property will want certainty regarding the level of cleanup needed and security that it won't be sued after conducting a cleanup.

Another opportunity for use of such agreements is in the context of an owner of commercial property that was contaminated by a dry cleaning tenant. Assume the property owner does not have the financial wherewithal to clean up the contamination and the tenant is

now judgment proof. It is unlikely that any prospective purchaser will agree to buy the property without liability protection. The owner of the property could consider approaching DEP with an offer to use the proceeds of the sale of the property to finance cleanup of the site, with the buyer obtaining liability protection. There are a variety of issues that must be considered by the practitioner, including the cost of cleanup and the value of the property if clean. If the anticipated cost of remediation (based on estimates prepared by an environmental consultant) indicate that the cost of cleanup is below the value of the parcel if clean, then the seller has an opportunity to attract a buyer who will know that the property it receives will meet a clean up standard acceptable to DEP and will obtain protection by way of a buyer-seller agreement. Under this scenario, DEP will require the seller to enter into a Consent Order and Agreement to conduct the cleanup using the proceeds of the sale. The seller and DEP must also negotiate the terms of the buyer-seller agreement, which will be attached as an exhibit to the CO&A and will define for prospective purchasers their obligations. Examples of a CO&A and Buyer Seller Agreement involving this scenario are attached.