

White Paper: Why Would a Buyer Require an Environmental Assessment?

***Takeaway:** For "bricks and mortar", companies or those that offer products or services associated with chemicals or commodities, a buyer is sure to require an environmental assessment. Understand what this assessment is, and how you can prepare for one.*

When you are selling a business, a buyer will typically require a "Phase One" environmental report as part of their due diligence process. This is a standard process if you are either selling the real estate along with your business, or leasing the real estate to the buyer. The buyer requires a Phase One environmental report primarily to support its financing requirements since the real estate would be used as security for the financing. This is typically a non-issue for you, the seller, unless there are major problems with the site i.e. asbestos, oil leaks, PCP's. If there are problems, the buyer may order a Phase Two report, back out of the deal completely, or most likely look for a haircut on the purchase price to "allow for the correction of the issues identified."

If you're selling this type of business, you need to be aware of this. You can manage the Phase One by attending the site visits, and identifying the issues first and crafting a risk mitigation plan. This can save you a few dollars if there are actually any problems. Also, remember that the buyer will most certainly look for seller indemnifications in the purchase and sale agreement against any previous environmental liabilities, so you are going to carry this risk anyways. Therefore, why get a haircut on the purchase price? The use of a Phase One is often used by some buyers as a technique to drive the purchase price down, so beware.

What is a Phase One Environmental Report?

It is a high-level review of potential areas of environmental concern that would need further looking into.

They provide a high level diagnostic and determine if a Phase Two assessment is required. Preferably not, as Phase Two's are only required when there's a problem and

the full environmental impact and financial cost needs to be quantified. The Phase One usually identifies areas of potential environmental concern ("APEC's"), and then ranks their risk as low, moderate, or high. Only if there is a high risk will a buyer be concerned. I have found that very seldom is a Phase Two report required if you get in front of the process and take ownership of any environmental risks early.

The assessment will usually be conducted in two ways:

1. By visiting the site and conducting interviews; and
2. By conducting a review of external documents with various agencies.

What the assessor is looking is for two distinct types of potential environmental risk:

1. Risk of potential contamination from onsite land use; and
2. Risk of contamination that may be caused from offsite sources such as adjacent property, utilities, or underground pipelines, wells, etc.

The On-site Visit

The assessor will therefore first conduct an onsite visit and interviews where the focus will be primarily on:

1. Identify any above and below ground storage tanks to see if there is potential for leaks - even if there are no leaks present, this is an almost automatic low to moderate risk identified as there is always "the potential" for leaks even if none are observed.
2. Vegetation review, ponding of water, and general erosion - if the vegetation around the site is looking a bit sad or there is erosion around it, the assessor will likely note as an area to follow up.
3. Existence of asbestos, polychlorinated biphenyls ("PCB's" which could come from leaks in electrical transformers for example), mold, ozone depleting substances ("ODS"), lead, urea formaldehyde foam insulation ("UFFI's"), etc. - All

of these are pretty nasty contaminants which likely would trigger an immediate Phase Two (if I were buying or leasing your property, I would ask for a Phase Two). The good news is that if the building was constructed after 1982, the chances of finding any of these nasties considerably decreases. If you are aware of them, have a containment and mitigation plan already in place BEFORE the Phase One occurs. Don't assume the Phase One won't find or identify this, it will, it's part of their checklist.

4. 4. Existence of any chemical storage - again this is an automatic low to moderate risk even if there are no leaks evident. Be ready to show that you have secondary containment in place.
5. 5. Existence of transformers, piping, air conditioning, elevators, or other mechanisms that may leak any contaminant fluids.

The Offsite Review

For the off-site review, the assessor would likely conduct a number of regulatory enquiries to assess if there is exposure to contamination from other sources by reviewing the following:

1. If there are above or below ground tanks, then the City or State Tank Management Association may be contacted to ensure these are registered.
2. The federal or state energy board will be contacted to determine if there are any oil/gas wells or pipelines within the general proximity of the site that may represent a contamination risk.
3. The city or town health services board may also be contacted to see if there are any outstanding complaints or orders against the owners of the real estate regarding any contamination.
4. Aerial photographs going back a few decades may be ordered to see if the site had any previous land uses that are subject to potential contamination (think gas station 40 years ago).



Don't Be Alarmed if a Buyer Requests One - It's Par for the Course

When you are preparing your business for sale, especially if you intend to package the real estate in the transaction, don't be surprised if a Phase One Environmental Report is commissioned. It is almost a given that it will, so don't panic. The key is to be prepared and conduct your own process prior to the assessor visiting the site. Make sure that you have identified yourself any of the potential issues noted above, and you have a plan in place to solve the problem. This goes a long way to giving you some bargaining leverage with the buyer in the event the Phase One environmental report is used as ammunition to drive a haircut in the purchase price.

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