



Why "Due Diligence?"

by Keane Callahan

Due to increased liability risks associated with environmental pollution or code violations, verifying the regulatory compliance of a commercial or industrial facility - or even a house -- is becoming standard pre-purchase practice in real estate transactions. This practice is called "due diligence." Particularly for larger projects, it can require the assistance of an attorney, engineer, or environmental consultant.

Why is due diligence necessary? Why bother with the expense and effort needed to find out whether the property complies with all applicable laws and regulations?

The answer is obvious. Without investigating state or local regulations, a potential buyer runs the risk of

Undertaking due diligence helps determine whether all regulatory requirements have been satisfied by the seller. Without investigating all these state or local regulations, a buyer runs the risk of "buying a violation" and ultimately being financially responsible for correcting it.

"buying a violation" and ultimately being financially responsible for correcting it. Undertaking due diligence will help determine whether all applicable regulatory requirements have been satisfied by the seller. For example, a due diligence investigation may reveal that a seller of residential property altered an on-site wetland and watercourse without state or local approvals. Similarly, purchasing an industrial facility may expose a potential buyer to expensive hazardous waste clean-up or pollution abatement measures.

Creating a Checklist

Due diligence is best accomplished through an established, systematic procedure designed to collect all pertinent land use and environmental information. The most critical step of this procedure is developing a comprehensive yet flexible checklist that outlines applicable federal, state, and

municipal laws, statutes, regulations, ordinances, and permit requirements that may apply to the particular project. The checklist also may be used to discover or verify previous violations, enforcement actions, or pollution abatement orders associated with the property. Although the checklist may vary depending upon the type of land use or real estate transaction, a standard checklist may include some or all of the following considerations.

Federal environmental requirements. These may include:

- U.S. Army Corps of Engineers wetland permit approval pursuant to Section 404 of the Clean Water Act;
- Environmental Protection Agency hazardous waste reporting requirements;
- National Pollutant Discharge Elimination System permit, for discharge of pollution into water bodies;
- Air pollution control permit pursuant to the Clean Air Act; and/or
- Environmental Impact Statement requirements pursuant to the National Environmental Policy Act.

The federal checklist also may include laws and statutes regulating disposal of solid waste, development in coastal zones, preservation of historic structures or archaeological sites, or construction of energy-producing facilities.

State laws and regulations. These may require some or all of the following:

- Water pollution control permit;
- Water diversion permit;
- Registration of or permit to construct a dam;
- Registration of or permit to install underground storage tanks;
- Air pollution control permit;
- Traffic control approval; and/or
- Coastal development approval for the placement of fill in tidal wetlands or for dredging.

Municipal requirements and regulations. These might include:

- Planning and zoning approvals such as site plan approval, subdivision approval, or special permit approval;
- Determination of potential zoning nonconformity problems such as setback encroachments, excess lot coverage, or inadequate road frontage;
- Inland or freshwater wetland approval;
- Water and sewer connection permits;
- Building permits, certificates of occupancy, and certificate of zoning compliance;

- Domestic drinking well permit; and/or
- Septic system permit.

Refining the Paperwork

Once the master checklist is developed, an attorney, consulting engineer or planner, or building contractor typically consults with the client to determine the exact parameters of the due diligence. This is basically a matter of refining the checklist. The checklist may become more focused or expanded to include additional laws or regulations applicable to a specific purchase. Once the precise parameters of due diligence are determined, the checklist is revised accordingly, and the task of checking the items begins.

The Legwork

The next step is to contact the appropriate regulatory agencies that have authority over the project. These may include agencies that range from the U.S. Army Corps of Engineers to your local public works department. All appropriate files, records, and maps are reviewed. Agency personnel often are interviewed to gain additional insight about the project.

The Homework

The fourth step of the due diligence process is making sense of all the information you've collected. It involves reviewing the requirements of all laws or regulations that apply and figuring out whether the project, based on its specifications and your assembled information, meets the requirements. This step also determines whether all necessary approvals have been granted and if there are any outstanding permit violations, or whether additional research is needed.

Writing the Report

The final step is getting it down on paper. A due diligence report presents a factual summary of the land use and environmental regulatory status of the project. It can help you in deciding whether to buy a particular piece of land, in negotiating the purchase price, or in acquiring financing for the purchase. Most importantly, it provides the assurance that the regulatory homework has been done and that the project's legal and regulatory risks have been identified and accounted for. ■

Keane Callahan is an environmental analyst in the Land Use and Environmental Section of Robinson & Cole, a 125-lawyer firm with offices in Hartford and Stamford, Conn. If you have legal questions you'd like to see addressed in this column, write to: Legal Column, The Journal of Light Construction, RR 2, Box 146, Richmond, VT 05477.