



Why Phase I Environmental Site Assessments Aren't Enough

Most clients buying or leasing a property that may have environmental issues, such as contamination from hazardous substances or petroleum products, understand that a Phase I Environmental Site Assessment (ESA) is necessary. Not only does the bank require it for financing, but the underwriter may require it before coverage is issued.

However, most general liability insurance policies often exclude pollution-related losses. And unless your client is prepared to address these losses out-of-pocket, they will want to consider more holistic environmental insurance.

This applies even to properties with clean Phase I ESA. While a Phase I ESA is designed to help insureds avoid legal liability for pre-existing contamination, it is not considered a comprehensive review – and carries its fair share of blind spots.

CONTACT

To learn more about how Amwins can help you place coverage for your clients, reach out to your local Amwins broker.

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Please refer to your policy for the actual language.

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The basics of a Phase I ESA

The American Society of Testing and Materials (ASTM) Phase I ESA assesses environmental conditions of commercial properties and should be completed within the first 180 days of owning a property. This standardized assessment is meant to help identify the presence of surface and subsurface contaminants and protect landowners from third-party toxic tort claims or liability asserted by state or local entities.

To complete the first step of the assessment, an environmental professional (EP) who meets ASTM requirements will conduct a site visit, evaluate on-site records and examine any historical documentation.

Next, the EP will interview employees and other individuals knowledgeable about both current and historical activities on the property. A third-party provider will summarize federal, state and tribal records to create a database of information about not only the property, but its surrounding areas as well. To create this database, the provider will also refer to historical resources, such as topographic maps and fire insurance maps. The final step is to write the report, documenting the information as well as any sources used.

Non-scope considerations such as lead-based paint and drinking water, as well as materials containing asbestos and radon, are technically outside of the scope of a Phase I ESA, but a thorough Phase I will consider them regardless. It's important to remember that the new owner of the property should pay for the assessment. If the former owner orders the report, the insured will not have protection from the Comprehensive Environmental Response, Compensation & Liability Act (CERCLA) via the bona fide prospective purchaser (BFPP) defense.

The pitfalls of a Phase I ESA

A Phase I ESA does not account for any activities at the property that occur after its publication. For example, mold exposure as the result of water damage could occur after the Phase I ESA is crafted and reviewed.

Additionally, events that are considered safe at the time of a Phase I ESA's publication could evolve into scenarios that create liability. For example, the increased occurrence of severe weather events such as flooding opens new avenues of risk for properties and property owners may be held liable for cleaning up contamination that initially occurred in a different location but was transported to the property in question through a flood or tornado.




Another example of why Phase I ESAs may not constitute a strong legal defense includes the fact that the report is only as strong as the data and information provided to the EP. The term "Significant Data Gap" was coined by the ASTM to address situations when missing information impedes the EP's ability to identify risks. Unfortunately, a Phase I ESA could easily overlook a recognized environmental condition (REC).



How to strengthen a Phase I ESA



Before your Phase I ESA report is finalized, be sure to request a draft report. If possible, ask for a verbal report immediately following the initial site visit. This can help prepare for next steps if any RECs are found and begin work on a Phase II ESA immediately.

If a Phase II study is ordered, this deeper dive will help identify RECs by:

-  Sampling soil and groundwater
-  Testing samples for contaminants of concern (COC)
-  Testing for vapor intrusion

If contamination is discovered, further sampling and testing are typically performed to help determine the full scope of the contamination on the property.

Similarly, you may consider supplementing a Phase I ESA with:

-  A title search for any recorded environmental cleanup liens
-  A search for activity use limitations on the property (e.g., deed restrictions limiting property use to commercial or industrial uses only or prohibiting the use or installation of groundwater wells)

With both types of searches, the onus to initiate them is on the prospective buyer or property owner and not the EP. Both searches are typically excluded from a Phase I ESA.

When a Phase I ESA isn't enough

These three real-life cases demonstrate why a Phase I ESA should not be considered an insured's sole legal defense. Loopholes in most general liability policies leave large coverage gaps that can prove costly for whomever is held liable for damages.

All three cases illuminate the need for comprehensive environmental insurance policies that cover pollution and contamination. A Phase I ESA would not have held up as a legal defense in any of these situations – the incidences occurred after the Phase I ESA would have been conducted.

Hydrochloric acid leak

When more than 5,000 gallons of hydrochloric acid leaked from a storage tank in Laurel, MS, the acid – which was originally liquid – created a cloud that traveled across the street to the plaintiff's property. The cloud caused damage to the plaintiff's buildings, equipment and inventory.

A unit of Travelers, the plaintiff's insurance company, **denied the claim** due to a pollution exclusion in its policy. There was an exception to the exclusion for losses caused by smoke, which the plaintiff tried to argue applied in this case due to the cloud of acid. However, the district court ruled that the cloud of acid did not qualify as smoke. The decision was unanimously upheld by a three-judge appeals court panel.

Mercury leak

Similarly, mercury was leaked during a science experiment at Putnam Middle School in Birmingham, AL, while a substitute teacher was leading the experiment. The substitute was not aware that the substance in question was mercury, so it wasn't discovered until a week later.

The Birmingham Board of Education was **deemed liable** for more than \$500,000 to clean up the school and investigate students' bookbags, clothes and homes. The district's insurance denied the claim for the mercury spill due to spills, seepage and contamination of any kind not being covered.

Toxic pesticide

In a third case, two individuals sued an Oklahoma City-based property company in state court, citing substantial harm from the company spraying pesticides that contained toxic chemicals. A unit of Chubb **refused to defend** the case due to a total pollution exclusion in its coverage.

When the property company tried to sue the Chubb unit for breaching its policy by refusing coverage and acting in bad faith, the U.S. District Court ruled in Chubb's favor. The decision was later upheld by an appeals court panel, who stated that the property company failed to prove that pollution was covered by the policy (as is required when a defendant is accused of acting in bad faith).

Filling the gap

Although most standard general liability policies have absolute pollution exclusions, it is possible to find pollution legal liability and help fill the gaps. This insurance can:

- Provide coverage for past, current and future environmental losses
- Cover business interruption losses that may occur alongside a pollution event
- Pair with mold liability and mold clean-up coverage for a more comprehensive policy

Amwins' environmental practice understands where and when environmental mitigation or risk transfer is needed. With expertise in industries as diverse as manufacturing, construction and healthcare, we know your clients' vulnerability to environmental losses and are focused on bringing you innovative solutions.

Contact your Amwins broker today for more information.

Insight provided by:

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