

# Innocent Landowner Programs and Their Effects on Environmental Risk and Property Value Impacts

by Thomas O. Jackson, PhD, MAI, and Jennifer M. Pitts

**T**his edition of “Environment and the Appraiser” examines the growing use of state programs that protect owners or purchasers of properties that may be impacted by environmental contamination. These parties may be considered “innocent landowners” under many state laws if they meet certain requirements related to the contamination source and other factors. By participating in such programs, landowners and/or prospective purchasers are relieved of certain future liabilities related to the contamination and its remediation under applicable state standards.<sup>1</sup> As will be seen, this reduces environmental risk and potentially adverse effects on property values.<sup>2</sup>

As presented in Advisory Opinion 9 (AO-9), “The Appraisal of Real Property That May Be Impacted by Environmental Contamination,” *environmental risk* may be defined as “the additional or incremental risk of investing in, financing, buying and/or owning property attributable to its environmental condition.”<sup>3</sup> Much of this risk is related to uncertainties concerning future liabilities for remediation costs and responsibilities for those costs. In turn, *environmental stigma* is defined as “an adverse effect on property value produced by the market’s perception of increased environmental risk due to contamination.”<sup>4</sup> Accordingly, by

mitigating risks though innocent purchaser and/or landowner liability relief, the risk effects and adverse property value impacts of environmental stigma may be reduced.

## State Innocent Landowner Programs

As noted, a growing number of states are now instituting programs to facilitate the purchase and redevelopment of contaminated sites by innocent third parties. This column discusses the programs in two such states, Texas and Arizona, and explains several key differences between the two programs. Case studies are also presented involving contaminated properties that sold with the protections of the Texas program. The case studies illustrate the positive effect of innocent landowner programs on the sale price, value, and marketability of properties impacted by environmental contamination.

## Texas Innocent Owner/Operator Program

The State of Texas has been very proactive in encouraging the purchase and development of contaminated sites. In September 1997, Texas instituted the Innocent Owner/Operator Program (IOP) to mitigate the risks of environmental contamination to innocent parties. The Texas IOP provides a certificate to an innocent owner or operator whose prop-

1. The innocent landowner defense under the federal Superfund law was discussed in a previous edition of “Environment and the Appraiser,” see Thomas O. Jackson, “The EPA’s Proposed All Appropriate Inquiries Rule and the Appraisal of Contaminated Properties,” *The Appraisal Journal* (Spring 2005): 146–153.
2. As set forth in Advisory Opinion 9 (AO-9), there are three possible property value effects from contamination: cost effects or “deductions for costs to remediate a contaminated property”; use effects or “impacts on the utility of the site as a result of the contamination”; and risk effects as “derived from the market’s perception of increased risk and uncertainty.” Appraisal Standards Board, “The Appraisal of Real Property That May Be Impacted by Environmental Contamination,” *Uniform Standards of Professional Appraisal Practice*, 2005 ed., Lines 169–183 (Washington, DC: The Appraisal Foundation, Washington, 2005), 147.
3. *Ibid.*, 144–145; see also Thomas O. Jackson, “Appraisal Standards and Contaminated Property Valuation,” *The Appraisal Journal* (Spring 2003): 127–133.
4. Appraisal Standards Board, 145.

erty is contaminated solely as a result of the release or migration of contaminants from an off-site source. This Innocent Owner/Operator Certificate (IOC) releases the owner/operator from liability for all costs incurred during the investigation, monitoring, or remediation of contaminants. An example of this certificate is presented in the Appendix.

To be eligible for an IOC, an applicant must meet specific requirements. The applicant must be the current owner or operator of the subject property. The owner/operator also must demonstrate that the property is contaminated due to a release or migration from an outside source, and that the owner/operator did not cause or contribute to the contamination in any way. If the property was subdivided from the source property after September 1, 1997 (the effective date of the IOP law), the owner must further demonstrate that the property was not contaminated at the time of purchase, or that the owner did not know and had no reason to know of the contamination when the property was acquired. An owner/operator who meets all of these criteria is eligible to proceed with the application process. This process includes (1) completing a site investigation report; (2) submitting a completed application with a \$1,000 fee; (3) notifying adjacent landowners; (4) agreeing to provide access to the property when necessary; and (5) agreeing on restrictions necessary to protect human health and the environment.

**Site Investigation Reports.** A site investigation report (SIR) describes the area of concern and demonstrates that the property is contaminated due solely to an off-site release or migration. All applicants for an Innocent Owner/Operator Certificate must complete a Phase I SIR that identifies any potential sources of contamination, both on- and off-site. The Phase I SIR should include a complete operational history of the property, a list of documentation describing any potential contamination sources, copies of any documents describing chemical or waste treatment on the property, area maps, and aerial photographs. If the Phase I SIR data indicates potential on-site source areas of contamination, then a Phase II SIR must be completed that includes additional sampling of soil and groundwater. If no potential source areas are indicated on-site, then no additional sampling is necessary.

**Application and Fees.** If the completed SIR indicates that contamination is present from an off-site source and that the owner/operator has not contributed to or exacerbated this contamination, then an application form may be completed and submitted to the Texas Commission on Environmental Quality (TCEQ). The application includes information about the owner/operator, a legal description of the site, the completed SIR, and proof that the applicant meets all requirements and is eligible for an IOC. A \$1,000 application fee is required for all reasonable costs incurred in reviewing the application. The applicant will be billed quarterly if the actual costs exceed this fee, and any unused portion will be returned to the applicant once the application process is complete.

**Notice.** The owner/operator must notify all adjacent landowners that an IOC has been applied for within 14 days after an application is submitted. This allows all relevant parties to submit any additional information to the TCEQ regarding the contamination. If an applicant fails to notify all adjacent landowners, the application for an IOC will be denied.

**Property Access and Restrictions.** In addition to meeting all requirements and notifying all adjacent landowners, the applicant must sign an affidavit allowing reasonable access to the property for future investigation or remediation of contaminated soils and/or groundwater. The TCEQ may also condition the issuance of an IOC on the enactment of institutional controls. These controls may include deed restrictions that limit the allowable uses of the subject property. Restrictions will only be enacted when necessary to protect human health or the environment. If at any time an owner/operator refuses reasonable access or violates any restrictions, the IOC will be denied or revoked.

**Issuance of Certificate.** An IOC is not transferable to a future owner or operator of a property. A prospective owner or operator may apply for an IOC, but the IOC will not be issued until the applicant actually owns or begins operation of the site. Applications typically take less than 45 days to process. Parties may terminate participation in the program at any time by written notice. As of July 21,

2005, the TCEQ had received 507 applications for the IOP, covering a wide variety of property types, and 405 IOCs had been issued.

### **Arizona Prospective Purchaser Agreement**

The State of Arizona also has a program to protect innocent parties from environmental risks and liabilities. Unlike the Texas IOP, which offers protection to current owners and operators, the Arizona Prospective Purchaser Agreement is issued to potential purchasers of contaminated properties. According to state statute, the Arizona Department of Environmental Quality (ADEQ) may enter into a Prospective Purchaser Agreement (PPA) with a potential purchaser of a facility.<sup>5</sup> The PPA provides a written release of liability and covenant not to sue for existing contamination at the site. While only owners/operators of non-source properties are eligible for an IOC in Texas, prospective owners of both source and non-source properties in Arizona are eligible for a PPA, as long as the prospective purchaser did not contribute to contamination of the site.

Certain statutory conditions must be met in order for a PPA to be issued. First, the facility must be within a site identified on the Water Quality Assurance Revolving Fund registry, or sufficient information must be provided to the ADEQ to identify the extent of contamination at the site. Also, the prospective purchaser must not be currently liable for any contamination on the property and may not be affiliated with any other responsible party through a familial or contractual relationship. Furthermore, the proposed redevelopment or reuse of the property must not contribute to existing contamination, interfere with necessary remediation, or expose the public to any additional health risks. Most importantly, the agreement must result in a substantial benefit to the community.

**Public Benefit.** The requirement that a PPA must result in a substantial public benefit is a major factor that differentiates the Arizona PPA from the Texas IOC. The prospective purchaser must identify the specific public benefit that will be provided if the PPA is issued. The state statute provides that the public benefit may include any of the following:

(1) substantial funding to perform remedial measures at the site; (2) performance of substantial remedial measures at the site; (3) productive reuse of a vacant or abandoned property; (4) development of a site by a governmental entity or nonprofit organization to address an important public purpose; (5) creation of conservation or recreation areas; or (6) any other public benefit that the ADEQ considers sufficient.<sup>6</sup> Officials at the ADEQ assert that bringing an abandoned property into productive use is the most common public benefit of these agreements. Consequently, the PPA is especially useful in encouraging the redevelopment of brownfields.

**Fees and Public Notice.** There is currently a \$900 fee assessed for a typical PPA. Additional fees are charged if a property presents an unusual difficulty. The ADEQ must notify the public of a PPA through a local newspaper in the county where the property is located. The publication costs are the responsibility of the prospective purchaser and are not included in the \$900 fee. The prospective purchaser must also grant an easement to ADEQ and any authorized representatives for inspection or remediation of the property.

**Issuance of Agreement.** To be eligible for consideration of a PPA, a draft agreement of the PPA must be received by the ADEQ before closing occurs on the sale of the subject site. The ADEQ does not have the authority to prevent any other independent parties from pursuing claims. The PPA is null and void if the purchaser fails to perform any of the required statutory responsibilities. Unlike a Texas IOC, a PPA is assignable to future prospective purchasers who are eligible for the program.

### **Case Studies Involving Innocent Landowner Protections**

The positive effects of the liability relief and risk reduction through innocent landowner programs can be illustrated using case studies. Three case studies involving properties in the Texas IOP program are used for this purpose.

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5. Ariz. Rev. Stat. §49-285.01.

6. Ibid.

### Case Study One

The subject property in this case study was a retail strip center of 6,108 square feet on a site of 0.403 acres in Austin, Texas, that sold for \$650,000, or \$106.42 per square foot. The property had soil and groundwater contamination consisting of chlorinated solvents (perchloroethylene, or PCE, and trichloroethane, or TCE) released from an adjacent dry cleaner.<sup>7</sup> The buyer was “fully aware” of the contamination prior to the sale. There were monitoring wells in place, but no active remediation. The contamination was said to be naturally attenuating, or breaking down on its own.<sup>8</sup> As part of a prepurchase environmental assessment of the property, an SIR was prepared and an IOP was obtained in 2001 from the Texas Natural Resource and Conservation Commission (now the TCEQ). The buyer indicated that with the IOP, “contamination of this nature has little effect on the price, considering the source (dry cleaner) agrees to be responsible for any cleanup.”

To investigate this further, five unimpaired comparables were analyzed. The unimpaired comparables involved five sales of similar retail strip centers (similar age, size, use, and dates of sale) located within 10 miles of the subject property (similar locations and market). They were considered unimpaired in that they were not contaminated, or at least there were no reported contamination issues associated with the sales. The unit prices for the five unimpaired comparables were \$78.08, \$73.80, \$93.04, \$86.13, and \$104.99 per square foot of leasable area. These were the most directly comparable properties in the local market area. Accordingly, their unit prices can be compared to the subject, which sold for \$106.42 per square foot. A comparison of unit prices indicates no diminution in value. The impaired subject actually sold for slightly more than its unimpaired comparables.

### Case Study Two

The subject for this case study was an older industrial warehouse facility of 101,839 square feet located in the Dallas-Ft. Worth metroplex. The property sold for \$1.7 million, or \$16.79 per square foot. The property had

been marketed for a lengthy period, but sold quickly after an IOC was obtained. According to parties to the transaction, once the IOC was issued, there were “no problems finding buyers.” There were multiple potential sources for the contamination at this non-source subject property. A primary source site for the volatile organic compounds (including biodegraded TCE) and metals discovered in monitoring wells around the site was a former manufacturing facility on an adjacent site with leaking above-ground storage tanks. There was also reportedly a dry cleaner on another site that had a closed contamination issue. Significant investigation went into demonstrating to the TCEQ that the contamination on the subject property was not generated by any current or former tenants of the site. As noted, the Texas program applies only to non-source sites. The unit price for the subject property of \$16.79 per square foot was found to be within the market range for unimpaired comparables: \$16.16 to \$17.89 per square foot. This again confirms the positive effect of an IOC on property value and marketability.

### Case Study Three

This case study involves the sale of a vacant industrial site of approximately 5.5 acres in Dallas for \$712,800 or \$2.97 per square foot. The property was contaminated from an adjacent site that had been used as a truck stop. The groundwater and soil contamination consisted of petroleum hydrocarbons—namely benzene, toluene, ethylbenzene, and xylenes (BTEX) and MTBE—from leaking underground storage tanks at the adjacent former truck stop. The SIR confirmed that the subject property, which had been previously used as a concrete manufacturing facility, was not the source of the contamination. The subject property was vacant at the time of sale and was covered with concrete. There had been underground storage tanks on the subject property, but these had been removed, and the state agreed that these tanks were not the source of the hydrocarbon contamination on the property. The seller of the subject property had conducted the necessary studies and obtained an IOC (for the buyer) prior to the sale. The unit price of \$2.97 per square foot for the subject property was bracketed by market prices of \$2.13 to \$3.00 per square foot for unimpaired comparables,

7. The subject properties in the three case studies would be considered non-source properties in the framework of source, non-source, adjacent, and proximate properties in AO-9. Appraisal Standards Board, 145.

8. A discussion of monitored natural attenuation can be found in Thomas O. Jackson, “Case Studies Analysis: Environmental Stigma and Monitored Natural Attenuation,” *The Appraisal Journal* (Fall 2004): 111–118.

again indicating no diminution in value for a contaminated property with an IOC.

### **Conclusion**

Innocent landowner programs are beneficial not just for individual property owners, but also for the communities in which the properties are located. These mechanisms can help facilitate brownfield redevelopment efforts and turn underutilized properties into productive uses. This has positive effects on the surrounding market area and local tax base. As explained, the reduction in potential future liabilities for remediation of contaminated sites has the effect of mitigating environmental risk to the market in general and buyers of these properties in particular. Reductions in risk and uncertainty concerning liabilities and costs would then reduce any environmental stigma impacts on property values. This was evident in the three case studies presented, which demonstrated increased marketability and the lack of any adverse price and value impacts subsequent to obtaining an IOC through the Texas program.

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**Appendix**

**TEXAS COMMISSION ON ENVIRONMENTAL QUALITY  
INNOCENT OWNER/OPERATOR PROGRAM CERTIFICATE**

As provided for in §361.753, Subchapter V, Solid Waste Disposal Act (SWDA), Texas Health and Safety Code.

I, JACQUELINE S. HARDEE, P.E., DIRECTOR OF THE REMEDIATION DIVISION, TEXAS COMMISSION ON ENVIRONMENTAL QUALITY (TCEQ OR COMMISSION), CERTIFY UNDER §361.753, SWDA, TEXAS HEALTH AND SAFETY CODE, THAT NECESSARY INVESTIGATIONS HAVE BEEN COMPLETED AS DESCRIBED IN THE APPROVED SITE INVESTIGATION REPORT(S) DATED KEYBOARD(DATES OF REPORTS) (SITE REPORT) FOR THE TRACT(S) OF LAND DESCRIBED IN EXHIBIT "A" (SITE), AND THAT KEYBOARD(NAME OF OWNER/OPERATOR) IS AN INNOCENT OWNER [OPERATOR] AS DEFINED BY §361.751(2) FOR THE SITE, BASED ON THE AFFIDAVIT FOR IOP NO. KEYBOARD(IOP NO.) IN EXHIBIT "B". A COPY OF THE SITE REPORT MAY BE FOUND IN THE TCEQ CENTRAL RECORDS OFFICE UNDER IOP NO. KEYBOARD(IOP NO.).

KEYBOARD(NAME OF OWNER/OPERATOR) IS NOT LIABLE UNDER THE TEXAS HEALTH AND SAFETY CODE OR THE TEXAS WATER CODE FOR INVESTIGATION, MONITORING, REMEDIATION OR CORRECTIVE OR OTHER RESPONSE ACTION S REGARDING THE CONDITIONS ATTRIBUTABLE TO THE RELEASE OR MIGRATION OF THE CONTAMINANT(S) IN KEYBOARD(LIST MEDIA) FROM A SOURCE OR SOURCES NOT LOCATED ON OR AT THE SITE INCLUDING: KEYBOARD(LIST CONTAMINANTS) DESCRIBED IN THE SITE REPORTS OR RELATED DEGRADATION PRODUCTS, OR OTHERWISE LIABLE REGARDING THOSE CONDITIONS. KEYBOARD(NAME OF OWNER/OPERATOR) SHALL GRANT REASONABLE ACCESS TO THE PROPERTY FOR PURPOSES OF INVESTIGATION AND REMEDIATION TO PERSONS DESIGNATED BY THE EXECUTIVE DIRECTOR OF THE TCEQ.

EXECUTED this \_\_\_\_ day of \_\_\_\_\_, 20 \_\_\_\_

\_\_\_\_\_  
Jacqueline S. Hardee, P.E., Director  
Remediation Division

STATE OF TEXAS  
TRAVIS COUNTY

BEFORE ME, on this the \_\_\_\_ day of \_\_\_\_\_, personally appeared Jacqueline S. Hardee, P.E., Director, Remediation Division, of the Texas Commission on Environmental Quality, known to me to be the person and agent of said commission whose name is subscribed to the foregoing instrument, and she acknowledged to me that she executed the same for the purposes and in the capacity therein expressed.

GIVEN UNDER MY HAND AND SEAL OF OFFICE, this the \_\_\_\_ day of \_\_\_\_\_, 20 \_\_\_\_

\_\_\_\_\_  
Notary Public in and for the State of Texas

**Appendix (continued)**

*EXHIBIT "A"*  
*TEXAS COMMISSION ON ENVIRONMENTAL QUALITY*  
*INNOCENT OWNER/OPERATOR PROGRAM*  
*LEGAL DESCRIPTION OF PROPERTY*  
*IOP No. \_\_\_\_*

The property belonging to KEYBOARD(Name of Owner/Operator) is a KEYBOARD(# of Acres) acre tract, more or less, located at KEYBOARD(Address, City) in the (Name) League (No.), Abstract (No.), recorded in Volume (No.), Page (No.) of the Deed of Records in KEYBOARD(County) County, Texas; said KEYBOARD(# of Acres) acre property is more particularly described as follows:

(Insert metes and bounds description here)



**Appendix (continued)**

**EXHIBIT "B"**  
**TEXAS COMMISSION ON ENVIRONMENTAL QUALITY**  
**INNOCENT OWNER/OPERATOR PROGRAM**  
**AFFIDAVIT BY INNOCENT OWNER/OPERATOR**

Before me, the undersigned authority, personally appeared KEYBOARD(Name of Owner/Operator), who, being by me duly sworn, deposed as follows:

My name is KEYBOARD(Name of Innocent Owner/Operator) and I am a representative of KEYBOARD(Company Name). I am of sound mind, capable of making this affidavit, and personally acquainted with the facts herein stated:

KEYBOARD(Name of Innocent Owner/Operator) is the KEYBOARD(owner/operator) of the Site located at KEYBOARD(Address, City, County) County, Texas. The physical boundaries of the site are set out in the attached Exhibit "A", "Legal Description of Property" (Site).

KEYBOARD(Name of Innocent Owner/Operator) has KEYBOARD(owned/operated) the Site from KEYBOARD(Enter Date) to KEYBOARD(Enter Date).

KEYBOARD(Name of Innocent Owner/Operator) or its representatives have completed investigations, pursuant to Section 361.753(a) of the Texas Solid Waste Disposal Act, at the Site described in Exhibit "A" to this certificate. The plans and reports submitted by KEYBOARD(Name of Innocent Owner/Operator) in its Innocent Owner/Operator Application contain information collected and analyzed using a prudent degree of inquiry consistent with accepted industry standards. The plans and reports are true, correct and complete to the best of my knowledge.

The Site has become contaminated as a result of a release or migration of contaminants in KEYBOARD(List Media) from a source or sources not located on or at the Site. These contaminants are described in the Site Investigation Reports for the Site dated KEYBOARD(SIR Date(s)) located in the TCEQ Central Records under KEYBOARD(IOP No.)

Neither I, KEYBOARD(Name of Innocent Owner/Operator), my agents, nor other persons, properties or operations for which I have legal responsibility, have caused or contributed to the source or source(s) of contamination at the Site.

Site Innocent Owner or Operator

By: \_\_\_\_\_  
Signature

\_\_\_\_\_  
Name (Printed or Typed)

SWORN TO AND SUBSCRIBED before me on the \_\_\_\_\_ day of \_\_\_\_\_, 20\_\_\_\_

\_\_\_\_\_  
(Notary)