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## Oh the Tides They Are a Changin': Climate Change, Due Diligence, and How the Standard of Care Should Change to Reflect the Current Technologies in Flood Mapping

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# **Oh the Tides They Are a Changin’: Climate Change, Due Diligence, and How the Standard of Care Should Change to Reflect the Current Technologies in Flood Mapping**

*Stephanie Wartelle\**

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## INTRODUCTION

In 2017, Hurricane Harvey caused nearly \$55 billion in damages to commercial real estate.<sup>1</sup> Science suggests that weather events like Harvey are only expected to increase in frequency due to climate change.<sup>2</sup> The ramifications of climate change will create globe-wide impacts, but certain geographical regions are particularly vulnerable.

Cities such as Houston face some of the greatest risks from climate change due to their location near the coast. Hollywood Hair and Nail Salon, located in Houston's Montrose neighborhood, was closed for days after Harvey's floodwaters devastated the region.<sup>3</sup> However, owner Reza Nouri continued to work, and he offered free haircuts at Houston's storm evacuee shelters, despite the devastating losses to his business.<sup>4</sup> The salon had no flood insurance because, according to the government, the building was not located in a flood zone.<sup>5</sup> The National Flood Insurance Program ("NFIP") offers businesses such as Hollywood Hair and Nail Salon insurance coverage for the risk of flooding.<sup>6</sup> However, many small businesses like the salon go without such insurance unless their mortgages or leases require it—either because their property does not fall within a

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1. Konrad Putzier, *Hurricane Harvey Put as Much as \$55 Billion Worth of Houston's Commercial Real Estate Underwater*, BUS. INSIDER (Sept. 2, 2017, 6:10 AM), <https://www.businessinsider.com/hurricane-harvey-55-billion-houston-commercial-real-estate-underwater-2017-9> [<https://perma.cc/VX8F-5Z4B>].

2. U.S. GLOB. CHANGE RES. PROGRAM, *FOURTH NATIONAL CLIMATE ASSESSMENT, VOLUME II: IMPACTS RISKS AND ADAPTATION IN THE UNITED STATES* (2018), [https://nca2018.globalchange.gov/downloads/NCA4\\_Report-in-Brief.pdf](https://nca2018.globalchange.gov/downloads/NCA4_Report-in-Brief.pdf).

3. Ernest Scheyder, *99% of Houston's Companies Are Small Businesses — and They're Struggling to Recover After Harvey*, BUS. INSIDER (Sept. 2, 2017, 12:17 PM), <https://www.businessinsider.com/r-houstons-small-businesses-dig-out-from-harveys-onslaught-2017-9> [<https://perma.cc/S3DC-G2PM>].

4. *Id.*

5. *Id.*

6. *See* 42 U.S.C. §§ 4001–4031.

flood zone on the government's flood maps or because the NFIP's coverage is often inadequate.<sup>7</sup>

This pattern of floods destroying uninsured, flood-prone properties is a symptom of a bigger problem currently facing the United States—the law does not require parties to appreciate the true flood risks associated with commercial real estate. This failure under the current law leads to real estate development in high-risk areas, which enables the spread of misinformation and inaccurate pricing.<sup>8</sup> For example, Miami, another coastal city, is expected to experience disastrous sea level rise and has already begun to feel the effects of climate change.<sup>9</sup> To illustrate this issue, one journalist posed as a potential buyer in the Miami real estate market and described her encounters with business owners and real estate agents in the area. The writer reported that both the owners and agents either downplayed or entirely rejected the idea that Miami real estate is in jeopardy, stating: “Amazingly, in the face of these incontrovertible facts about the climate the business of luxury real estate is chugging along just fine, and I wanted to see the cognitive dissonance up close.”<sup>10</sup>

The problem is not just confined to Houston or Miami—experts expect climate change to have a significant impact on both existing real estate and future transactions in commercial real estate worldwide.<sup>11</sup> The U.S. government conducted an assessment of the potential impact of climate change and concluded that by 2050 up to \$106 billion in real estate will exist below sea level.<sup>12</sup> Some of the most severe impacts of climate change may not manifest themselves until 2050, which coincides with the maturity

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7. Scheyder, *supra* note 3.

8. *Reports: Flooding Risk Could Devalue Florida Real Estate*, ASSOCIATED PRESS NEWS (Jan. 21, 2020), <https://apnews.com/article/e066e6b1c74488e61ab0d0b7b3a6a248> [<https://perma.cc/CC6T-JXL2>].

9. *Id.*

10. Sarah Miller, *Heaven or High Water: Selling Miami's Last 50 Years*, POPULA (Apr. 2, 2019, 12:30 PM), <https://popula.com/2019/04/02/heaven-or-high-water/> [<https://perma.cc/WK95-E2U4>]. The writer does not discuss any legal obligations related to real estate agents or attorneys. However, her article serves to illustrate that public perception of flood risk is generally much lower than scientists' measurement of the risk. *See id.*

11. U.S. GLOB. CHANGE RES. PROGRAM, *supra* note 2.

12. *Id.*

date of today's 30-year mortgages.<sup>13</sup> Many scientists opine that the only solution for residents in certain affected areas is to permanently relocate.<sup>14</sup>

Regardless of the political debate surrounding climate change, asset managers and bank directors are taking note of the growing problem. Notably, BlackRock, the world's largest asset manager, has begun implementing exit strategies for certain investments that "present a high sustainability-related risk."<sup>15</sup> A recent report by the U.S. Commodities Trade Commission stated that "U.S. financial regulators must recognize that climate change poses serious emerging risks to the U.S. financial system, and they should move urgently and decisively to measure, understand, and address these risks."<sup>16</sup>

To depict another example of the real estate market's controversial reaction to climate change, when mortgage lenders make a loan to a homeowner in a flood-prone area, lenders are more likely to repackage that mortgage into a security and sell it on the financial market.<sup>17</sup> Local lenders want to sell these securities because the lenders have more "soft information,"<sup>18</sup> or information gleaned from a familiarity with the area,

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13. Philip E. Karmel, J. Kevin Healy & Steven J. Poplawski, *Addressing Climate Change in Due Diligence for Real Estate Transactions*, BRYAN CAVE LEIGHTON PAISNER (May 20, 2020), <https://www.bclplaw.com/en-US/insights/addressing-climate-change-in-due-diligence-for-real-estate-transactions.html> [https://perma.cc/NDE3-YU3Y].

14. Christopher Flavelle et al., *U.S. Flood Strategy Shifts to 'Unavoidable' Relocation of Entire Neighborhoods*, N.Y. TIMES (Aug. 26, 2020), <https://www.nytimes.com/2020/08/26/climate/flooding-relocation-managed-retreat.html> [https://perma.cc/66HR-4T8S].

15. Andrew Ross Sorkin, *BlackRock C.E.O. Larry Fink: Climate Crisis Will Reshape Finance*, N.Y. TIMES (Jan. 14, 2020), <https://www.nytimes.com/2020/01/14/business/dealbook/larry-fink-blackrock-climate-change.html> [https://perma.cc/LUY7-47BC]. A high sustainability risk in this context is a climate-related risk, such as the risk that a company will have a high carbon footprint. *Id.*

16. *Release Number 8234-20: CFTC's Climate-Related Market Risk Subcommittee Releases Report, Managing Climate Risk in the U.S. Financial System*, COMMODITY FUTURES TRADING COMM'N (Sept. 9, 2020) [hereinafter *Release No. 8234-20*], <https://www.cftc.gov/PressRoom/PressReleases/8234-20> [https://perma.cc/GY6Y-CSC2].

17. Bennett McIntosh, *Coastal Banks Shed Risky Mortgages—Putting the Financial System at Risk*, HARV. MAG. (July 1, 2020), <https://harvardmagazine.com/2020/07/coastal-banks-are-selling-off-mortgages-threatened-by-rising-seas> [https://perma.cc/5Z3M-CPCL].

18. "Soft information" has been defined as "opinions, predictions, analyses and other subjective evaluations," as opposed to "hard information," which is "statements concerning objectively verifiable historical facts." Janet E. Kerr, *A Walk Through The Circuits: The Duty to Disclose Soft Information*, 46 MD. L.

about flood-prone areas compared to national banks and other non-local buyers.<sup>19</sup> As a result, local lenders understand the risk involved in collateralizing flood-prone property. Consequently, the lenders pass that risk off to less informed investors by selling the mortgage as a security.<sup>20</sup>

Additionally, commercial mortgage-backed securities (“CMBS”), which are investments that pool loans for office buildings, hotels, shopping centers, and more, are among the securities most exposed to flood risk because of the concentration of cities on the U.S. coast.<sup>21</sup> In 2017, Hurricane Harvey caused \$131 billion in damage and affected over 1,300 CMBS loans, which was 3% of the CMBS market in 2017.<sup>22</sup> Moreover, Hurricane Irma in that same year affected 2% of that market.<sup>23</sup> Experts estimate that 80% of the commercial property damaged by those two storms was outside of FEMA flood zones, meaning that many of the buildings affected were not adequately insured.<sup>24</sup>

The root of the problem regarding the lack of current, comprehensive information concerning flood risk is that national banks, along with insurance companies<sup>25</sup> and other players in the real estate market, determine flood risk by analyzing flood maps drawn by the Federal Emergency Management Agency (FEMA).<sup>26</sup> As will be discussed in this Comment, FEMA’s flood maps often guide where and how to build, whether building owners and renters need flood insurance, and how much risk mortgage lenders should take.<sup>27</sup> Nevertheless, these maps are outdated and provide very limited information on flood hazards, and as a result, are essentially incorrect.<sup>28</sup> This culminates in an asymmetry of information existing between those players who rely exclusively on the flood maps and

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REV. 1071, 1071 n.2 (1987) (quoting Schneider, *Nits, Grits, and Soft Information in SEC Filings*, 121 U. PA. L. REV. 254 (1972)).

19. McIntosh, *supra* note 17.

20. *Id.*

21. Kate Duguid & Ally Levine, *From New York to Houston, Flood Risk for Real Estate Hubs Ramps Up*, CLAIMS J. (June 29, 2020), <https://www.claimsjournal.com/news/national/2020/06/29/297923.htm> [<https://perma.cc/NC69-2VK2>].

22. *Id.*

23. *Id.*

24. *Id.*

25. McIntosh, *supra* note 17.

26. Karmel, Healy & Poplawski, *supra* note 13.

27. Christopher Flavelle et al., *New Data Reveals Hidden Flood Risk Across America*, N.Y. TIMES (June 29, 2020), <https://www.nytimes.com/interactive/2020/06/29/climate/hidden-flood-risk-maps.html> [<https://perma.cc/UJ5N-AXMF>].

28. *Id.*

those who do not.<sup>29</sup> Therefore, homeowners, builders, banks, insurers, and government officials nationwide make decisions with information that understates the true environmental risks.<sup>30</sup>

Federal law mandates that FEMA has a duty to provide comprehensive, up-to-date flood information and to consider the future impacts of climate change on flood hazards.<sup>31</sup> However, FEMA has failed to do so.<sup>32</sup> The good news is despite the absence of accurate, climate-driven information from FEMA, modern technology is now making it possible for private actors to accelerate the availability of this crucial information to the public.<sup>33</sup> Even more notable, courts and other legal authorities have a vital role to play in holding professionals accountable for disseminating outdated and incomplete information about risks to their clients.<sup>34</sup> Once the law recognizes the outdatedness characterizing most information parties rely on in evaluating flood risk and subsequently helps to remedy the situation, lenders and other professionals will look to sources besides FEMA maps for more accurate and reliable information.<sup>35</sup>

The legal avenue for ameliorating this predicament is known as “due diligence,” a legal concept used by transactional and real estate attorneys to refer to an investigation process.<sup>36</sup> The objective of due diligence is to obtain a professional opinion about the risks associated with a transaction

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29. Thomas Frank, *Studies Sound Alarm on “Badly Out-of-Date” FEMA Flood Maps*, SCI. AM. (Feb. 27, 2020), <https://www.scientificamerican.com/article/studies-sound-alarm-on-badly-out-of-date-fema-flood-maps/> [<https://perma.cc/KU9K-QR6B>].

30. Flavelle et al., *supra* note 27.

31. 42 U.S.C. § 4101b(b)(3)(D).

32. See *Coastal Flood Risk*, FEMA, <https://www.fema.gov/flood-maps/coastal> [<https://perma.cc/W2YN-2Q5Y>] (last updated Mar. 22, 2021).

33. Bob Jacobsen, *Real Flood Risk: The Grassroots Revolution*, BOB JACOBSEN PE 2, [https://883d608b-8c29-4fe3-8d4e-00f29484e05b.filesusr.com/ugd/04cf9d\\_1211b9d959b542d1b1d6c59395bb40bf.pdf](https://883d608b-8c29-4fe3-8d4e-00f29484e05b.filesusr.com/ugd/04cf9d_1211b9d959b542d1b1d6c59395bb40bf.pdf) [<https://perma.cc/UZ86-DR8L>] (last visited Aug. 18, 2021).

34. See discussion *infra* Part III.

35. See 427 Desk, *Climate Risk and Real Estate Investment Decision-Making*, FOUR TWENTY SEVEN (Feb. 7, 2019), <http://427mt.com/2019/02/07/climate-risk-and-real-estate-investment-decision-making/> [<https://perma.cc/F57A-5KUQ>] (stating that Heitman, a real estate manager, utilized 427’s climate risk exposure assessment technology); see also *Defining America’s Climate Risk*, FIRST ST. FOUND., <https://firststreet.org/> [<https://perma.cc/9UVS-UD92>] (last visited Aug. 18, 2021).

36. Andrew N. Jacobson, *A Narrative Real Estate Acquisition Due Diligence Checklist*, 17 PRAC. REAL EST. LAW. 7 (2001).

to remove any uncertainty prior to the actual purchase.<sup>37</sup> The duty to exercise due diligence stems from a fiduciary or professional-client relationship.<sup>38</sup> Accordingly, a failure to exercise due diligence can lead to claims that the professional fell below the applicable standard of care or breached their fiduciary duty.<sup>39</sup> Although a small group of commercial real estate players are becoming savvy enough to use the most up-to-date sources of information on flood prediction when advising clients, using such sources is well above the standard of care in exercising due diligence in the context of commercial real estate transactions.<sup>40</sup> This Comment will examine the issue of the outdated standard of care governing environmental due diligence and argue that courts should heighten the fiduciary or professional duty of agents involved in commercial real estate transactions to reflect the reality of expanding information on flood risk and climate change.

Accordingly, Part I of this Comment will provide background on the concept of due diligence and how it stems from a fiduciary duty associated with the attorney-client relationship.<sup>41</sup> Part II will demonstrate how present-day environmental due diligence is outdated.<sup>42</sup> Part III will propose a solution to this problem—one that urges courts to hold attorneys, or fiduciaries exercising environmental due diligence, to a higher standard of care than the low bar custom in the industry currently demands.<sup>43</sup>

## I. DUE DILIGENCE IN GENERAL

The phrase “due diligence” refers to a risk assessment performed by either a fiduciary or an attorney for the buyer or seller in a commercial real estate transaction.<sup>44</sup> There are multiple kinds of “due diligence,” such as

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37. John L. Payne, *Environmental Due Diligence*, 22 PRAC. REAL EST. LAW. 33 (2006).

38. See discussion *infra* Part I.

39. See discussion *infra* Part III.

40. Jacobsen, *supra* note 33.

41. See discussion *infra* Part I.

42. See discussion *infra* Part II.

43. See discussion *infra* Part III.

44. Annemargaret Connolly & Thomas D. Goslin, *Environmental Due Diligence in Real Estate Transactions*, RELX SDG RES. CENTRE (Sept. 2016), <https://sdgresources.relx.com/legal-practical-guidance/environmental-due-diligence-real-estate-transactions> [https://perma.cc/2GGS-RUJG].

financial, legal, business, and environmental.<sup>45</sup> The environmental due diligence process refers to an assessment of environmental risks.<sup>46</sup>

#### A. Due Diligence as Risk Management

To understand risk and how it relates to real estate transactions, it is necessary to first highlight the distinction between the terms “hazard” and “risk.” A “hazard” is anything that has the potential to cause harm.<sup>47</sup> The term “risk” refers to the *likelihood* that a hazard will cause harm.<sup>48</sup> Determining risk requires a consideration of whether how, and to what extent, a piece of property is exposed to a hazardous substance, condition, or activity.<sup>49</sup> Risks may be physical, such as flood risk, or non-physical, such as financial risk.<sup>50</sup>

There are essentially two types of risks associated with flooding caused by climate change: physical risks associated with flood damage and transition risks, also known as market-level risks.<sup>51</sup> Transition risks are related to market changes that occur as a result of increased flooding from climate change.<sup>52</sup> These risks include the possibility that markets vulnerable to climate change will have reduced economic activity, asset values that will decrease, and insurance costs that will increase.<sup>53</sup>

*Caveat emptor*—or “let the buyer beware”—is a concept that guides all real estate transactions and holds that the buyer accepts the risks of all

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45. Robert D. Frawley, *Due Diligence — The Crucible*, 218 N.J. LAW. 47, 48 (Dec. 2002).

46. *Id.*

47. *Risk vs. Hazard*, CAMPAIGN FOR ACCURACY IN PUB. HEALTH RES., <https://campaignforaccuracyinpublichealthresearch.com/risk-vs-hazard/> [<https://perma.cc/XG A7-V4UT>] (last visited Aug. 18, 2021).

48. *Id.*

49. *Id.*

50. Frawley, *supra* note 45.

51. *Climate Risk and Real Estate Investment Decision Making: New Report from ULI and Heitman*, HEITMAN (Feb. 5, 2019), <https://www.heitman.com/news/climate-risk-and-real-estate-investment-decision-making/> [<https://perma.cc/HJR 2-KN7L>].

52. *Id.*

53. *Id.* With respect to flood insurance, coverage limits for commercial properties are low, only offering \$500,000 for damage to real property and \$500,000 for damage to personal property. Additional property damage coverage and business interruption coverage may be available from excess carriers, but premiums are likely to rise over time with the additional flooding risks. *See* Karmel, Healy & Poplawski, *supra* note 13.

defects in the property not expressly assumed by the seller.<sup>54</sup> The general concept of due diligence stems from *caveat emptor* because purchasers assume most of the risks associated with property defects.<sup>55</sup> Consequently, purchasers are responsible for conducting due diligence analyses of the property before purchase.<sup>56</sup> Buyers' failure to exercise due diligence to protect themselves from property defects or other conditions in the property or deed can lead to a bar on subsequent claims against the seller for conditions the buyer should have discovered prior to the purchase.<sup>57</sup>

### *1. The Due Diligence Process in Real Estate Transactions*

The process of conducting due diligence bears even more significance and detail in the context of commercial real estate transactions. To manage risk in real estate transactions, the standard of practice dictates that both buyers and lenders exercise due diligence prior to signing a purchase contract.<sup>58</sup> In the context of commercial real estate transactions, due diligence is defined as "the inspection and investigation of . . . a business entity before a buyer makes the final decision whether to consummate an acquisition."<sup>59</sup> The buyer's goal in conducting due diligence is to fully understand the seller's business including its markets, customers, financial condition, legal position, and any other risks inherent in acquiring and operating the business.<sup>60</sup> Due diligence, therefore, is essentially a risk assessment.

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54. John R. Nolan, *Land Use and Climate Change Bubbles: Resilience, Retreat, and Due Diligence*, 39 WM. & MARY ENV'T L. & POL'Y REV. 321, 349 (2015).

55. *Id.*

56. *Id.*

57. *Due Diligence in Commercial Real Estate Transactions*, WOLTERS KLUWER (Mar. 23, 2021), <https://www.wolterskluwer.com/en/expert-insights/due-diligence-in-commercial-real-estate-transactions> [<https://perma.cc/M4CH-3Y4G>]. A concept that is directly tied to this is the seller's general duty of disclosure of relevant facts such as physical characteristics of a property, including easements, encumbrances, and other restrictions. *Id.* However, the disclosure duty is often more limited in the context of a commercial transaction as opposed to residential. *See id.* As such, it will not be discussed further by this Comment.

58. *Id.*

59. Levin v. May, 887 So. 2d 497, 501 (La. Ct. App. 2004) (quoting Jacobson, *supra* note 36, at 7).

60. *Id.* at 502 (citing Frawley, *supra* note 45).

Due diligence is employed in several types of real estate transactions, including simple real estate purchases.<sup>61</sup> It is also conducted in large corporate transactions such as real estate acquisitions, loan transactions secured by real estate, commercial leases, and corporate-level transactions that include significant real estate assets.<sup>62</sup> The due diligence considerations vary depending on the type of transaction.<sup>63</sup> The purchase agreement should include a period for due diligence with sufficient time to inspect the property.<sup>64</sup> After the property inspection, the buyer may decide not to purchase the property, attempt to negotiate an indemnity provision to shift financial responsibility for an environmental risk, or adjust the purchase price.<sup>65</sup> In some instances, the buyer may choose to obtain environmental insurance as protection.<sup>66</sup>

## 2. Parties Who Exercise Due Diligence

In the specific context of commercial real estate transactions, there are several professionals who exercise due diligence. These include sellers and buyers, any attorneys acting as agents for either party, environmental consultants, insurance agents providing insurance on the risk, and any real estate agents acting on behalf of the buyer.<sup>67</sup> Often, the lender is the driving force behind an environmental due diligence audit.<sup>68</sup> Most banks, insurance companies, and investors require that the purchaser, often a borrower, determine environmental risks associated with the property

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61. Robert L. Falk et al., *Environmental Due Diligence in Real Property Transactions*, 234 ENV'T. COUNS. 1 (2008).

62. Jacobson, *supra* note 36.

63. Falk et al., *supra* note 61. For example, a parent company acquiring ownership in a company that holds real property assets via the purchase of stock may not necessarily be liable for violations of certain environmental statutes by the subsidiary if they ensure the integrity of a parent-subsidiary relationship. In contrast, if a corporate transaction involves a merger, the acquiring party may be liable for such statutory violations of the acquisition's target company. Therefore, due diligence should include inspection of facilities belonging to the acquisition's target company. *Id.*

64. *Id.*

65. *Id.*

66. *Id.*

67. John L. Payne, *Environmental Due Diligence: Determining the Type and Amount of Data to Gather for Multiple Locations*, SS003 ALI-ABA 1647, 1650–51 (2010).

68. John L. Payne, *Gathering Data for Environmental Due Diligence*, 28 PRAC. REAL EST. LAW. 27, 28 (2012).

before obtaining a loan.<sup>69</sup> The borrower typically incurs the costs of the audits, either outright or in the loan costs imposed by the lender.<sup>70</sup> Sometimes, the seller performs the environmental audit and then provides the findings to the buyer's representative for review prior to submission to the lender.<sup>71</sup>

Buyers and sellers will perform due diligence before closing to understand the potential risks associated with a property and use that information to negotiate a price.<sup>72</sup> Additionally, as will be discussed further below, the property owner may have financial responsibility for the environmental condition of the property even though the owner may not have caused the contamination.<sup>73</sup> Thus, it is imperative due diligence be conducted thoroughly and extensively. Most environmental due diligence includes tasks that may need to be completed by an environmental advisor in conjunction with attorneys.<sup>74</sup> The environmental consultant collects the information for the audit that will be used to negotiate the deal.<sup>75</sup> The attorneys are tasked with analyzing the potential liabilities associated with a property, such as those arising from noncompliance with environmental statutes.<sup>76</sup> The attorneys may also oversee the review of permit compliance; the review of files and records of the owner, governmental agencies, and occupants; and the analysis of investigation results.<sup>77</sup> To further understand an attorney's responsibility in performing due diligence, it is necessary to examine the fiduciary relationship that creates the duty to exercise due diligence.

#### *B. The Fiduciary Relationship: The Source of the Duty to Exercise Due Diligence*

The duty to exercise due diligence stems from either a fiduciary duty or a duty to render competent legal representation. A fiduciary relationship exists between an agent and a principal when the agent is under a duty to act on behalf of or to give advice for the benefit of the principal upon matters within the scope of their relationship.<sup>78</sup> For example, in *EBC I, Inc.*

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69. *Id.*

70. *Id.*

71. *Id.*

72. *See id.*

73. *Id.* at 29.

74. *Id.*

75. *Id.*

76. *Id.*

77. Falk et al., *supra* note 61.

78. RESTATEMENT (SECOND) OF TORTS § 874 cmt. a (AM. L. INST. 1979).

*v. Goldman Sachs*, the Court of Appeals of New York found that an underwriter owed a fiduciary duty to a startup company by virtue of the underwriter offering advice for the benefit of the company.<sup>79</sup> The court noted that the company relied on the underwriter's expertise to advise the company on a fair offering price and to act with the company's best interests in mind.<sup>80</sup>

Fiduciary relationships appear in legal contexts such as contracts, wills, and trusts. These relationships arise in non-legal contexts as well, such as the elections of individuals like corporate directors.<sup>81</sup> Fiduciary duties fall into two broad categories: the duty of care and the duty of loyalty.<sup>82</sup>

The duty of care encompasses an agent's duty to act with the care, competence, and diligence normally exercised by agents in similar circumstances.<sup>83</sup> The duty of loyalty, by contrast, comprises the following: (1) an agent's duty not to acquire a material benefit from a third party in connection with transactions conducted on behalf of the principal; (2) an agent's duty to refrain from competing with the principal; (3) an agent's duty to avoid conflicts of interest; and (4) an agent's duty of confidentiality.<sup>84</sup>

The attorney-client relationship imposes a fiduciary duty on the attorney as well as a duty to competently represent the client.<sup>85</sup> Not every instance of professional negligence or malpractice results in a breach of fiduciary duties.<sup>86</sup> Scholars have distinguished a breach of a professional duty and a breach of a fiduciary duty in the following way: Professional

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79. *EBC I, Inc. v. Goldman, Sachs & Co.*, 832 N.E.2d 26, 32 (N.Y. 2005) (noting that “[w]e do not suggest that underwriters are fiduciaries when they are engaged in activities other than rendering expert advice”).

80. *Id.*

81. See Tamar Frankel, *Definition of “Fiduciary Duties”*, 2 THE NEW PALGRAVE DICTIONARY OF ECONOMICS AND THE LAW 127, 127–28 (Peter Newman ed., 1998), <https://cyber.harvard.edu/trusting/unit5all.html> [<https://perma.cc/9Y6A-FCW6>].

82. *Id.* The duty of care is distinct from the duty of loyalty, as the former is a duty of performance, while the latter is a duty of honesty. Some, but not all, courts label duties of care as “fiduciary.” See, e.g., *Oxford Shipping Co., v. N.H. Trading Corp.*, 697 F.2d 1, 6 (1st Cir. 1982). Further, some statutes label the duty of care as “fiduciary.” See, e.g., REV. UNIF. P’SHIP ACT § 404(a) (1997) (“The only fiduciary duties a partner owes to the partnership and the other partners are the duty of loyalty and the duty of care set forth in subsections (b) and (c).”).

83. RESTATEMENT (THIRD) OF AGENCY § 8.08 (AM. L. INST. 2006).

84. *Id.* §§ 8.02–.05.

85. 7A C.J.S. *Attorney & Client* § 367 (2020).

86. *Id.*

negligence by an attorney implicates a standard of care for competent representation, while a breach of a fiduciary duty implicates a duty of loyalty and honesty.<sup>87</sup> Put another way, the attorney has two principal duties: the duty to competently represent the client and the duty to comply with fiduciary obligations.<sup>88</sup> A breach of the former is professional negligence, or legal malpractice in the case of attorneys.<sup>89</sup>

Most courts categorize a claim asserting a failure to exercise due diligence as a legal or professional malpractice claim, but plaintiffs sometimes assert both a claim of breach of a fiduciary duty and a claim of professional or legal malpractice.<sup>90</sup> Further, the attorney has an ethical duty to competently and diligently represent their client.<sup>91</sup> While a breach of this ethical duty does not necessarily dictate the standard of care in a malpractice case, it is often considered as relevant evidence to the standard of care for attorneys.<sup>92</sup> By contrast, in the case of other fiduciary relationships besides the attorney-client relationship, courts characterize a

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87. *See id.* There has been some confusion among courts in distinguishing a breach of fiduciary duty claim from a professional negligence claim. *See id.* This is because the duty to exercise care has been cited as one of the fiduciary duties outside the context of professional malpractice. *See cases cited supra* note 83. By contrast, courts have stated that an attorney's fiduciary duty only encompasses the obligations of "fidelity, honesty, and good faith." *Pippen v. Pederson & Houpt*, 986 N.E.2d 697, 704 (Ill. App. Ct. 2013). Regardless, the focus of this Comment is that both can be implicated in an allegation of a failure to exercise environmental due diligence.

88. *See* 2 RONALD E. MALLEEN, LEGAL MALPRACTICE § 15:3 (2020 ed.), Westlaw LMAL.

89. *Id.* In the context of legal malpractice, the standard of care pertains to the requisite knowledge, skill, and diligence of an attorney. *Id.*

90. *See, e.g., Coves of the Highland Comm. Dev. Dist. v. McGlinchey Stafford PLLC*, No. 09-7251, 2010 WL 4340921, at \*1 (E.D. La. Oct. 21, 2010) (asserting claims of legal malpractice, negligence, breach of fiduciary duty, and negligent misrepresentation against a law firm for its alleged failure to conduct "environmental due diligence" in connection with the bond proposal documents); *Moguls of Aspen, Inc. v. Faegre & Benson*, 956 P.2d 618, 621 (Colo. App. 1997) (holding that a requested jury instruction on breach of fiduciary duties was not warranted in legal malpractice action against attorney and law firm in connection with advice concerning termination of clients' lease of commercial property; the claims were essentially failure to exercise due diligence claims and only implicated a malpractice action).

91. MODEL RULES OF PRO. CONDUCT r. 1.3 (AM. BAR ASS'N 2019).

92. Kathleen J. McKee, Annotation, *Admissibility and Effect of Evidence of Professional Ethics Rules in Legal Malpractice Action*, 50 A.L.R. 5th 301 § 3 (1997).

failure to exercise due diligence as a breach of a fiduciary duty.<sup>93</sup> The difference in theories under which claims are brought is a theoretical one, but the distinction has a few practical implications: A breach of a fiduciary duty may sound more egregious than a breach of the duty of care, and a negligence claim may be time-barred before the claim for breach.<sup>94</sup> Thus, the plaintiff will often attempt to bring both.<sup>95</sup>

### *C. Custom and the Standard of Care for Due Diligence*

In determining whether conduct falls below the standard of care or violates a fiduciary duty, the custom of the community in question, or other similar communities, is a relevant factor for courts to consider.<sup>96</sup> A custom may be common to the community in general, or it may consist of the shared practices of a relatively small group of persons who engage in particular activities.<sup>97</sup> Regardless of whether the duty to exercise due diligence constitutes a professional or fiduciary duty, courts will look to custom to discern whether an agent breached their duty to exercise due diligence.<sup>98</sup> This is because the fiduciary duty of care encompasses an agent's duty to act with the care, competence, and diligence normally exercised by agents in similar circumstances, and custom speaks to what is normally done by agents in similar circumstances.<sup>99</sup> Further, malpractice is a negligence claim, one element of which is a breach of the standard of care.<sup>100</sup> The standard of care dictates what is reasonable under the circumstances, and custom is often relevant in assessing the standard of care.<sup>101</sup>

Custom, however, is not dispositive as to the question of malpractice or breach of a fiduciary duty when a reasonable person would not follow it.<sup>102</sup> A famous case from the United States Court of Appeals for the Second Circuit illustrates this point.<sup>103</sup> In *The T.J. Hooper*, cargo owners sued the owner of barges that sank in a storm, and the barge owner then

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93. See *Anwar v. Fairfield Greenwich, Ltd.*, 826 F. Supp. 2d 578, 589 (S.D.N.Y. 2011).

94. MALLEN, *supra* note 88.

95. *Id.*

96. See RESTATEMENT (SECOND) OF TORTS § 295 (AM. L. INST. 1965).

97. *Id.* cmt. a.

98. See *id.*

99. RESTATEMENT (THIRD) OF AGENCY § 8.08 (AM. L. INST. 1965).

100. RESTATEMENT (SECOND) OF TORTS § 295 cmt. a (AM. L. INST. 1965).

101. See *id.* § 295.

102. *Id.* cmt. a.

103. See *The T.J. Hooper*, 60 F.2d 737 (2d Cir. 1932).

sued the owner of the tugs that towed the barges.<sup>104</sup> The tugs were not equipped with working radio sets.<sup>105</sup> Although use of radio sets was not yet common in the industry, the court held that the tug owners were negligent.<sup>106</sup> The court stated that custom is often equivalent to the standard of proper care or diligence.<sup>107</sup> However, it is not dispositive in determining whether a party breached the standard of care.<sup>108</sup>

The court reasoned that if the utility of a certain safety precaution outweighs the cost of taking such precaution, then failure to implement that precautionary measure constitutes negligence.<sup>109</sup> Indeed, the court noted that a “whole calling may have unduly lagged in the adoption of new and available devices.”<sup>110</sup> The court furthered that no industry or trade can be permitted to set its own uncontrolled standard at the expense of the community.<sup>111</sup> The policy reason underlying this rule is clear: If the custom of an industry dictates the applicable standard of care, then no incentive exists to increase the safety measures utilized by that industry.<sup>112</sup>

The custom among professionals conducting environmental due diligence is outdated as it does not recognize the current realities of climate change, especially in the context of flooding. This outdatedness is rooted in the origins of environmental due diligence as a defense to liability under environmental statutes. In assessing the current state of environmental due diligence, an understanding of its statutory origins is necessary.

## II. ENVIRONMENTAL DUE DILIGENCE AND ITS OUTDATEDNESS

In the context of commercial transactions, liabilities may arise from environmental statutes or common law.<sup>113</sup> To preserve liability defenses

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104. *Id.*

105. *Id.* at 739.

106. *Id.* at 740. The court decided the question of unseaworthiness, a maritime term which describes the condition of a vessel. *See id.* Though not identical, it can be equated to negligence.

107. *Id.*

108. *Id.*

109. *See id.*; *see also* RESTATEMENT (SECOND) OF TORTS § 295 cmt. a (AM. L. INST. 1965). This is known as the Learned Hand formula, or BPL. B is the burden of implementation, P is the probability of the loss (or the risk), and L is the gravity of the loss. Where  $PL > B$ , the defendant has breached the duty of care. *See United States v. Carroll Towing Co.*, 159 F.2d 169, 173 (2d Cir. 1947).

110. *The T.J. Hooper*, 60 F.2d at 740.

111. *Id.*

112. RESTATEMENT (SECOND) OF TORTS § 295 cmt. a (AM. L. INST. 1965).

113. *See* Jeff Civins & Mary Mendoza, *Transactional Environmental Due Diligence: What Diligence is Due*, 20 NAT. RES. & ENV'T 22, 22 (2006).

and manage environmental risks associated with properties contaminated with hazardous substances or petroleum, purchasers of real estate, tenants, and their lenders all perform due diligence on the property.<sup>114</sup> Historically, the primary focus of such environmental due diligence inquiries was the risks associated with hazardous substances as well as the target property's compliance with applicable environmental regulations.<sup>115</sup>

#### *A. The Statutory Origins of Environmental Due Diligence*

The concept of environmental due diligence originated from the need to evaluate whether a potential asset was contaminated with hazardous substances.<sup>116</sup> The law giving rise to liability in such cases is the Comprehensive Environmental Response, Compensation, and Liability Act ("CERCLA," also known as "Superfund") of 1980.<sup>117</sup> CERCLA discourages parties from acquiring, financing, and developing properties contaminated with hazardous substances by imposing strict liability on potentially responsible parties ("PRPs").<sup>118</sup> These PRPs include present owners and operators of a site contaminated by hazardous substances, owners and operators of the site at the time of disposal of the hazardous substances, transporters who selected the site, and generators of waste who arranged for its disposal at the site.<sup>119</sup> CERCLA liability is both strict and unlimited.<sup>120</sup> In addition, CERCLA allows "other persons," such as current facility owners, to seek reimbursement from PRPs for any necessary response costs that the private parties have incurred.<sup>121</sup> Congress intended CERCLA's liability scheme to provide incentives for private parties to investigate potential sources of contamination and initiate remediation efforts.<sup>122</sup>

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114. Lawrence P. Schnapf, *Environmental Due Diligence in the Era of Climate Change*, 24 PRAC. REAL EST. LAW. 49, 50 (2008).

115. Karmel, Healy & Poplawski, *supra* note 13.

116. See Douglas Feichtner, *It's Not Just About CERCLA Anymore: Evolving Climate Change Regulations Create New Aspects of Environmental Due Diligence*, 29 ANDREWS ENV'T LITIG. REP. 1 (2009).

117. *Id.*

118. Civins & Mendoza, *supra* note 113, at 23 (citing 42 U.S.C. § 9601).

119. Feichtner, *supra* note 116, at 1; Civins & Mendoza, *supra* note 113, at 23 (citing 42 U.S.C. § 9607(a)).

120. Civins & Mendoza, *supra* note 113, at 23..

121. 42 U.S.C. § 9607(a)(4)(B).

122. See *Cadillac Fairview/Cal., Inc. v. Dow Chem. Co.*, 840 F.2d 691, 694 (9th Cir. 1988).

Originally, there were three defenses a PRP could assert to avoid liability under CERCLA: (1) an act of God; (2) an act of war; and (3) an act or omission by a third party.<sup>123</sup> In 1986, the Superfund Amendments and Reauthorization Act transformed the “act or omission” defense into the innocent landowner (“ILO”) defense.<sup>124</sup> The ILO defense focuses on parties to a real estate transaction. Under this defense, the PRP needs to show—among other requirements—that it acquired the property *after* disposal of the hazardous substances, and at the time of acquisition the PRP did not know and did not have reason to know that any hazardous substances were disposed of at the facility.<sup>125</sup> To show that a party had no reason to know about the disposal of any hazardous substances at the time of the acquisition, the party must show it conducted “all appropriate inquiries [“AAI”] . . . into the previous ownership and uses of the facility in accordance with generally accepted good commercial and customary standards and practices.”<sup>126</sup> Environmental due diligence, therefore, was simply the standard to measure the reasonableness of the investigation into the property or whether a party made AAI into the facility. The EPA describes AAI as “the process of evaluating a property’s environmental conditions and assessing potential liability for any contamination.”<sup>127</sup> Subsequent amendments to CERCLA created additional defenses that could not be asserted by a party unless they had first performed due diligence in the form of AAI.<sup>128</sup>

In *United States v. A & N Cleaners & Launderers, Inc.*, the U.S. brought an action to hold three individuals who purchased a commercial building in 1979—before Congress enacted CERCLA—liable for environmental response costs.<sup>129</sup> The court applied CERCLA retroactively and held that the purchasers were not entitled to rely on the innocent purchaser defense under CERCLA, in part, because they failed to conduct

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123. Civins & Mendoza, *supra* note 113, at 23.

124. *See id.*; 42 U.S.C. § 9601(35)(A).

125. Civins & Mendoza, *supra* note 113, at 23 (citing 42 U.S.C. §§ 9607(b)(3), 9601(35)(A)(i)).

126. *Id.* (citing 42 U.S.C. § 9601(35)(B)(i)(1)).

127. *Brownfields All Appropriate Inquiries*, EPA, <https://www.epa.gov/brown-fields/brownfields-all-appropriate-inquiries> [<https://perma.cc/JLY2-MFB9>] (last visited Aug. 23, 2021).

128. *See* 42 U.S.C. §§ 9601(35)(A) (Innocent Landowner Defense), 9601(40) (Bona Fide Purchaser Defense), 9607(q) (Contiguous Landowner Defense).

129. *See U.S. v. A & N Cleaners & Launderers, Inc.*, 854 F. Supp. 229, 243 (S.D.N.Y. 1994).

due diligence prior to purchasing.<sup>130</sup> The court noted that the purchasers did not sufficiently inquire into the property's history and should have: (1) inquired about the previous property owner's disposal practices; (2) questioned environmental officials on the status of the property; and (3) inquired into the legality of the disposal practices of their tenants and subtenants.<sup>131</sup> Importantly, local newspapers published that the city government was investigating the source of the contamination, and the purchasers had even consented to an investigation of their property.<sup>132</sup> As a result, the court noted that the purchasers' failure to investigate the property was inexcusable since they were aware of the risk of contamination of the property.<sup>133</sup>

Although AAI was once an amorphous standard,<sup>134</sup> the EPA eventually clarified that AAI now requires a "Phase I site assessment" as established by the American Society for Testing and Materials.<sup>135</sup> Every Phase I environmental site assessment must be conducted in compliance with the rules promulgated by the EPA.<sup>136</sup> There are multiple methods of satisfying the requirements for conducting a sufficient Phase I site assessment.<sup>137</sup> AAI requires an environmental professional to oversee the process and sign off on the environmental report.<sup>138</sup>

As noted by the EPA, the AAI Phase I assessment includes specific activities such as interviews with past and present owners, operators, and occupants; review of historical sources of information; review of records from federal, state, tribal, and local governments; visual inspection of the facility and adjoining property; review of commonly known or reasonably ascertainable information; assessment of the degree of obviousness of the

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130. *See id.* at 238. The court discusses the "Due Care and Precautionary Requirements" under 42 U.S.C. § 9601(35)(A). The due care requirement is the same as the due diligence requirement, which looks to the "all appropriate inquiries" standard. The precautionary requirement outlined in 42 U.S.C. § 9601(A)(II) is the requirement that the defendant took reasonable steps to prevent further release of the hazardous substance.

131. *Id.* at 243.

132. *Id.*

133. *Id.*

134. *See id.* at 241 ("The only blameworthy activity that many property owners facing CERCLA liability have engaged in is the failure to comply with the host of amorphous and undefined due care requirements necessary for establishing CERCLA's affirmative defenses.").

135. *See* 40 C.F.R. § 312.11 (2018).

136. *See id.* § 312.

137. *See id.* § 312.20.

138. *Id.*; *see id.* § 312.10(b)(1) (defining "Environmental Professional").

presence or likely presence of contamination at the property; and the detection of contamination.<sup>139</sup>

The AAI requirement to review public records refers to either federal, state, or local government records that include reports of incidents of previous spills and sites identified as contaminated.<sup>140</sup> However, AAI requires more than just a review. It also requires on-site inspection, and where an inspection is impracticable, a review of imagery such as aerial photographs of the property.<sup>141</sup> These photographs are referred to as historical sources of information.<sup>142</sup> A third-party vendor usually obtains these historical aerial photographs, and the buyer then reviews them collectively to observe as much of an area's past as possible to develop a historical understanding of the property.<sup>143</sup>

In one instance, Gabriel Environmental Services, an environmental consulting firm, used these photographs to conduct a Phase I site assessment.<sup>144</sup> While reviewing the aerial photos, the firm found that the photographed site was undeveloped in 1949, by 1970 had been developed into a gas station, and by 1990 had been redeveloped for use as a strip mall.<sup>145</sup> The 1970 aerial photo was the key historical documentation that showed there may be petroleum products present at the site.<sup>146</sup> Although at the time the EPA had developed a database to find areas with both active and closed underground storage tanks,<sup>147</sup> no other governmental documentation of underground storage tank removal or soil sampling

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139. U.S. ENV'T PROT. AGENCY, EPA-560-F-19-179, ALL APPROPRIATE INQUIRIES FINAL RULE (2017) [hereinafter ALL APPROPRIATE INQUIRIES FINAL RULE], [https://19january2021snapshot.epa.gov/sites/static/files/2017-07/documents/aa\\_i\\_factsheet\\_final\\_rule\\_epa\\_560\\_f\\_17\\_195\\_508.pdf](https://19january2021snapshot.epa.gov/sites/static/files/2017-07/documents/aa_i_factsheet_final_rule_epa_560_f_17_195_508.pdf) [<https://perma.cc/J79A-CD46>].

140. 40 C.F.R. § 312.26 (2020).

141. *Id.* § 312.27(c).

142. ALL APPROPRIATE INQUIRIES FINAL RULE, *supra* note 139.

143. Brianna Sadoski, *The Importance of Evaluating a Property's Historical Uses During Environmental Due Diligence*, EHS SUPPORT (Oct. 9, 2018), <https://ehs-support.com/news/the-importance-of-evaluating-a-property-s-historical-uses-during-environmental-due-diligence/> [<https://perma.cc/KG4J-225Z>].

144. *Phase I Environmental Site Assessment Spotlight: Aerial Photographs*, GABRIEL ENV'T SERVS. [hereinafter *Phase I*], <https://gabrielenvironmental.com/phase-i-environmental-site-assessment-spotlight-aerial-photographs/> [<https://perma.cc/NC8R-PNYY>].

145. *Id.*; *UST Finder*, EPA, <https://www.epa.gov/ust/ust-finder> [<https://perma.cc/9LZW-7QNV>] (last visited Aug. 23, 2021).

146. *Phase I*, *supra* note 144.

147. *UST Finder*, *supra* note 145.

existed for this particular site.<sup>148</sup> Standard environmental due diligence, therefore, has long recognized that scrutiny of government data and maps may not always suffice to ascertain the actual amount of risks associated with a property. The standard of care for conducting environmental due diligence as a defense to CERCLA liability may demand that a party look to sources of information beyond what the government provides, such as the aerial photos utilized by Gabriel. Despite this increased rigor in the context of CERCLA, the standard for environmental due diligence in other areas has unfortunately not followed suit.

### *B. Contemporary Environmental Due Diligence*

Today, following AAI is standard practice, and parties adhere to it in nearly every commercial transaction.<sup>149</sup> In addition to AAI, however, environmental due diligence may also include risk assessments associated with asbestos, lead-based paint, lead in drinking water, radon, mold, and more.<sup>150</sup> The standard for AAI looks backward by analyzing the past risks associated with a property and thus is not designed to address unexpected risks that may materialize from climate change in the future.<sup>151</sup>

Even in CERCLA's early stages, courts recognized that "willful or negligent ignorance about the presence of or threats associated with hazardous substances" does not excuse a PRP's noncompliance with the due diligence requirement created by CERCLA's defenses.<sup>152</sup> However, this intolerance for willful or negligent ignorance of certain risks did not translate into the flood-risk assessment context; in other words, climate change-related flood risk is often not included in many environmental due diligence analyses.<sup>153</sup> As will be discussed in Section D of this Part, when a party to a commercial real estate transaction assesses flood risk, it usually does so with outdated and inaccurate governmental resources. This reliance on governmental information is due in part to the difficulty in quantifying flood risk.<sup>154</sup> Further, environmental risks associated with

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148. *Phase I*, *supra* note 144.

149. *See Schnapf*, *supra* note 114, at 49.

150. *See id.*

151. *See Karmel, Healy & Poplawski*, *supra* note 13; *see also Civins & Mendoza*, *supra* note 113, at 24.

152. *U.S. v. A & N Cleaners & Launderers, Inc.*, 854 F. Supp. 229, 243 (S.D.N.Y. 1994).

153. *See Connolly & Goslin*, *supra* note 44.

154. *See id.*

climate change are often seen as more remote than other risks and typically develop over long periods of time.<sup>155</sup>

The risks posed by climate change, particularly in the context of flooding, are potentially greater than any risks associated with environmental liability, so it is unacceptable that the commonplace avenues for meeting the AAI standard of environmental due diligence overlook such impactful risks.<sup>156</sup> Though these risks do not carry with them any form of statutory liability, they may be significant to a buyer or investor and, if overlooked or misreported, could form the basis for malpractice liability.<sup>157</sup>

### *C. The Risk of Flooding Encompassed by Environmental Due Diligence*

In assessing flood risk during the process of environmental due diligence, the standard of practice among professionals in commercial real estate transactions typically involves scrutiny of flood maps published by FEMA.<sup>158</sup> Thus, it is not within the current standard of care to look outside of these governmental maps. Generally, a court will consider the standard of practice in an industry as the relevant standard of care unless it is unreasonable to do so.<sup>159</sup> FEMA is the federal agency that administers the National Flood Insurance Program (NFIP).<sup>160</sup> Congress created the NFIP in 1968 with the National Flood Insurance Act,<sup>161</sup> and the NFIP serves as the primary source of flood insurance for residential properties in the

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155. C. Gregory Rogers, *Environmental Disclosure Due Diligence: The Next Step in Environmental Due Diligence*, BUS. L. TODAY 31, 32 (2007).

156. See *Release No. 8234-20*, *supra* note 16.

157. See TASK FORCE ON CLIMATE RELATED DISCLOSURES, FINAL REPORT: FINAL RECOMMENDATIONS OF THE TASK FORCE ON CLIMATE-RELATED FINANCIAL DISCLOSURES (2017) [hereinafter TASK FORCE], <https://www.fsb-tcfd.org/publications/final-recommendations-report/#> [<https://perma.cc/9V7B-WLJZ>] (discussing the significant risk that climate change poses to financial markets, noting that many organizations incorrectly perceive this risk).

158. Karmel, Healy & Poplawski, *supra* note 13.

159. See *The T.J. Hooper*, 60 F.2d 737 (2d Cir. 1932). There is a lack of jurisprudence in this specific area of law that would indicate the standard of care in a malpractice action for a failure to exercise due diligence regarding climate change-related risks. However, there is a likelihood that these types of malpractice actions may happen more frequently as climate-change-related risks become more imminent and measurable.

160. 42 U.S.C. § 4011(a).

161. See National Flood Insurance Act, Pub. L. No. 90-448, title XIII, § 1302 (1968).

U.S.<sup>162</sup> Additionally, it is utilized by commercial actors in the industry to determine flood risk.<sup>163</sup> The NFIP has two main policy goals: (1) to provide access to primary flood insurance, thereby transferring some of the financial risk of property owners to the federal government and (2) to mitigate the nation's flood risk through the development and implementation of standards for managing floodplains.<sup>164</sup> Currently, there are 22,403 communities that participate in the NFIP, which has written an estimated 5.1 million policies with \$1.3 trillion of insurance in force.<sup>165</sup>

The three basic components of the NFIP are: (1) the identification and mapping of flood-prone communities; (2) the requirement that communities adopt and enforce regulations for floodplain management so as to meet certain eligibility criteria to qualify for flood insurance; and (3) the provision governing flood insurance.<sup>166</sup> This Comment focuses primarily on the first of the three components since the NFIP's flood maps play an important role in the process of discharging environmental due diligence in commercial real estate transactions.

The goal behind the first component of the NFIP is the development of flood maps across a majority of the country that specifies which areas are at a high risk of flooding.<sup>167</sup> However, FEMA has produced flood maps covering only one-third of the nation's 3.5 million miles of streams and only 46% of the country's shoreline.<sup>168</sup> The NFIP also requires communities participating in its insurance program to adopt and enforce a set of ordinances for floodplain management that are consistent with FEMA's minimum requirements.<sup>169</sup> Finally, property owners located in areas of the NFIP map designated as flood-prone are required to purchase flood insurance as a prerequisite to receiving a mortgage from a federally backed lender.<sup>170</sup> To comply with this requirement, property owners may

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162. DIANE P. HORN, CONG. RSCH. SERV., IF10988, A BRIEF INTRODUCTION TO THE NATIONAL FLOOD INSURANCE PROGRAM (2021).

163. See Karmel, Healy & Poplawski, *supra* note 13.

164. See *id.*

165. *The Watermark-National Flood Insurance Program Financial Statements*, FEMA, <https://www.fema.gov/flood-insurance/work-with-nfip/watermark-financial-statements> [<https://perma.cc/CS9U-UM5E>] (last visited Aug. 23, 2021).

166. *Nat'l Wildlife Fed'n v. Fed. Emergency Mgmt. Agency*, 345 F. Supp. 2d 1151, 1154–55 (W.D. Wash. 2004).

167. See 42 U.S.C. § 4101.

168. ASS'N OF STATE FLOODPLAIN MANAGERS, FLOOD MAPPING FOR THE NATION 3 (2020), [https://asfpm-library.s3-us-west-2.amazonaws.com/FSC/MapNation/AS\\_FPM\\_MaptheNation\\_Report\\_2020.pdf](https://asfpm-library.s3-us-west-2.amazonaws.com/FSC/MapNation/AS_FPM_MaptheNation_Report_2020.pdf).

169. 42 U.S.C. § 4102.

170. *Id.* § 4012a(b)(1).

purchase flood insurance through the NFIP or through a private company as long as the private flood insurance “provides flood insurance coverage which is at least as broad as the coverage” of the NFIP.<sup>171</sup> The lender, rather than FEMA, reinforces this mandate to procure flood insurance.<sup>172</sup>

#### *D. The NFIP’s Outdatedness*

The NFIP’s flood mapping is critical, as it forms the basis of the NFIP regulations and flood insurance requirements.<sup>173</sup> The problem with the NFIP’s current mapping system is that it is both outdated and inaccurate.<sup>174</sup> This inaccuracy is rooted in the way that the NFIP maps characterize areas as either prone to flood risk or not.

The NFIP maps implement what experts call a “binary approach” to predicting flood risk.<sup>175</sup> This approach determines that a property is either at risk or not at risk based on one criteria: whether the property falls within the 100-year floodplain, within the 500-year floodplain, or outside of those areas.<sup>176</sup> Areas within the 100-year flood zone are said to have a 1% annual chance of flooding, meaning they are at risk of flooding in the eyes of the NFIP.<sup>177</sup> Areas within the 500-year floodplain are said to have 0.2% annual chance of flooding, or a low risk of flooding.<sup>178</sup> The NFIP refers to areas outside the 500-year floodplain as “areas of minimal flood hazard.”<sup>179</sup> Homes and businesses in the 100-year floodplain with mortgages from government-backed lenders are required to have flood insurance.<sup>180</sup> The statute calls these areas “special flood hazards.”<sup>181</sup> On the other hand, flood insurance is merely recommended for properties within the 500-year floodplain.<sup>182</sup>

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171. *Id.* § 4012a(b).

172. *See* HORN, *supra* note 162.

173. *Flood Maps*, FEMA, <https://www.fema.gov/flood-maps> [<https://perma.cc/B6MB-5WJ4>] (last visited Aug. 23, 2021).

174. Frank, *supra* note 29.

175. Jacobsen, *supra* note 33.

176. *Id.*

177. *What Does the 500 Year Flood Mean?*, WTG FLOOD RES. CTR. (Mar. 2, 2017), <https://www.jdsupra.com/legalnews/flood-insurance-commercial-real-estate-44260/> [<https://perma.cc/HJ9D-SUXB>].

178. *Id.*

179. Karmel, Healy & Poplawski, *supra* note 13 (citing FEMA, *NFIP Glossary*, FEMA, <https://www.fema.gov/glossary/flood-zones> [<https://perma.cc/28FU-NWN8>]).

180. 42 U.S.C § 4012a.

181. *Id.*

182. *What Does the 500 Year Flood Mean?*, *supra* note 177.

Experts contend the NFIP maps place excessive emphasis on mapping this single 100-year flood zone area, resulting in a misleading binary classification that characterizes property as either at risk of flooding or not based on its location inside or outside this one area.<sup>183</sup> The current practice among lenders of requiring flood insurance only for properties with exposure to the 100-year flood reinforces this false, binary dichotomy.<sup>184</sup> The NFIP maps do not reveal the large uncertainties in the estimates of flood risk for properties within the 100-year flood zone—even for the most recent maps—and as a result the NFIP undervalues premiums in many high-risk areas and overprices them in others.<sup>185</sup>

Additionally, in many cases, the NFIP maps are outdated and fail to acknowledge the ways that changing climatic and developmental patterns have significantly shifted the risk of flooding.<sup>186</sup> For example, the NFIP maps do not take into account future increased rainfall,<sup>187</sup> although climate change has indeed increased rainfall and resulting flooding.<sup>188</sup> NFIP policyholders are also paying premiums that do not reflect the true risk of flooding in areas where they live because the NFIP maps fix their rates, and those maps do not accurately track the true risk of flooding.<sup>189</sup> Notably, the Natural Resources Defense Council authored a petition for rulemaking in January of 2021 for FEMA to amend its regulations implementing the NFIP, which includes amending the maps.<sup>190</sup>

Attorneys and other professionals involved in environmental due diligence currently have no reason to report information on the risks of flooding other than what they learn from the NFIP maps, as the standard of care for environmental due diligence accepts such information as

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183. Jacobsen, *supra* note 33.

184. *Id.*

185. *Id.*

186. See R.J. Lehmann, *Do No Harm: Managing Retreat by Ending New Subsidies*, R ST. (Feb. 20, 2020), <https://www.rstreet.org/wp-content/uploads/2020/02/195.pdf> [<https://perma.cc/4A24-C9R4>].

187. Laura Bliss, *The Dangerous Flaw in Flood Risk Maps*, BLOOMBERG CITY LAB (Sept. 2, 2016, 2:41 PM), <https://www.bloomberg.com/news/articles/2016-09-02/fema-flood-risk-maps-fail-to-account-for-future-climate-changes> [<https://perma.cc/7SYB-YUTA>].

188. See *Release No. 8234-20*, *supra* note 16.

189. Lehmann, *supra* note 186.

190. See ASS'N OF STATE FLOODPLAIN MANAGERS, INC., NAT. RES. DEF. COUNCIL, PETITION REQUESTING THAT THE FEDERAL EMERGENCY MANAGEMENT AGENCY AMEND ITS REGULATIONS IMPLEMENTING THE NATIONAL FLOOD INSURANCE PROGRAM (2021), <https://www.nrdc.org/sites/default/files/petition-fema-rulemaking-nfip-20210105.pdf>. The petition provides a more comprehensive discussion on the inaccuracies with the NFIP flood maps. See *id.*

adequate. Therefore, courts should raise the standard of care to require attorneys and other professionals to report accurate and updated information to clients.<sup>191</sup> After all, it is hardly diligent to relay to a client risks that outright ignore the realities of climate change.

### III. MODERNIZING THE STANDARD OF CARE FOR ENVIRONMENTAL DUE DILIGENCE

Scrutiny of the NFIP's flood maps should not be enough to absolve the environmental consultant or attorney from liability for damages resulting from a client's reliance on inadequate environmental due diligence. Attorneys who represent purchasers or buyers in commercial real estate transactions have a fiduciary duty to advise their clients of the risks associated with their prospective investments.<sup>192</sup> As such, they may face liability for failing to perform due diligence while representing and advising clients in property transactions.<sup>193</sup> This liability results from claims based on a breach of fiduciary duty or legal malpractice.<sup>194</sup>

*Barnett v. Schwartz* provides an example of a malpractice action concerning a failure to advise on environmental risks.<sup>195</sup> In *Barnett*, a client sued his attorney for legal malpractice based on the attorney's negligent failure to advise on the risks associated with a piece of commercial property before closing on the lease.<sup>196</sup> The attorney never informed his client that the property owner had committed environmental violations or that the sale was subject to an "as is" clause.<sup>197</sup> The appellate court affirmed the lower court's finding of malpractice, noting that the plaintiffs were "entitled to such information before entering into the agreement."<sup>198</sup> Similarly, a client may be entitled to information on flood-risk as well as climate change-related flood risk so as to be aware of the risks associated with the property to be purchased. It follows that an attorney's failure to relay these risks might be equally negligent.

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191. See discussion *infra* Part III.

192. Nolan, *supra* note 54, at 349.

193. 2 RONALD E. MALLIN, LEGAL MALPRACTICE § 24:46 (2020 ed.), Westlaw LMAL.

194. See *Coves of the Highland Comm. Dev. Dist. v. McGlinchey Stafford, P.L.L.C.*, 526 F. App'x 381 (5th Cir. 2013).

195. See *Barnett v. Schwartz*, 848 N.Y.S.2d 663, 664–65 (N.Y. App. Div. 2007).

196. *Id.*

197. *Id.* at 665.

198. *Id.*

*A. The Standard of Care for Environmental Due Diligence*

Attorneys have been sued for their failure to recommend an environmental investigation and for their failure to adequately handle environmental hazards in the discharge of due diligence.<sup>199</sup> For example, an attorney's failure to recommend an environmental consultant before his client purchased a gas station resulted in the client suing the attorney for legal malpractice.<sup>200</sup> Though this Comment focuses on attorney liability, environmental consultants—who typically alert purchasers of potential CERCLA liability—also could face liability for their negligence in the performance of an environmental assessment as part of the due diligence process.<sup>201</sup>

A case from the Louisiana Fifth Circuit Court of Appeal supports the notion that attorneys may indeed face liability for failure to exercise environmental due diligence.<sup>202</sup> In *Coves of Highland Community Development District v. McGlinchey Stafford, P.L.L.C.*, the real estate developer, Coves, sued its bond counsel, McGlinchey Stafford, for breach of fiduciary duty and legal malpractice.<sup>203</sup> The developer premised both claims on McGlinchey's alleged failure to discharge its duty to exercise environmental due diligence, which allegedly would have revealed issues relating to the property's prior use.<sup>204</sup> However, the court held that pursuant to the parties' agreement, Coves and McGlinchey did not intend

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199. See MALLEN, *supra* note 193 (citing SCB Diversified Mun. Portfolio v. Crews & Assocs., No. 09–7251, 2012 WL 13708 (E.D. La. Jan. 4, 2012) (granting summary judgment in favor of law firm because environmental due diligence was not within the scope of the retention); Kram Knarf, LLC v. Djonovic, 903 N.Y.S.2d 386 (N.Y. App. Div. 2010) (alleging failure to advise of due diligence regarding extent of contamination); Int'l Electron Devices (USA) LLC v. Menter, Rudin & Trivelpiece, P.C., 898 N.Y.S.2d 388 (N.Y. App. Div. 2010) (failing to recommend environmental investigation before closing); Eck v. Kellem, 748 N.E.2d 1047 (Mass. App. Ct. 2001) (alleging failure to protect seller adequately from environmental cleanup liability); Dixon Ticonderoga Co. v. Estate of O'Connor, 248 F.3d 151 (3d Cir. 2001); Kaplan v. Shure Bros., Inc., 153 F.3d 413 (7th Cir. 1998) (holding the legal malpractice claim was barred by statute of limitations)).

200. See Lanziano v. Cocozziello, 304 N.J. Super. 616 (App. Div. 1997).

201. James W. Spertus, *Holding Environmental Consultants Liable for Their Negligence: A Proposal for Change*, 64 S. CAL. L. REV. 1143 (1991) (arguing that an environmental consultant's liability to the purchaser is too limited).

202. See *Coves of the Highland Comm. Dev. Dist. v. McGlinchey Stafford, P.L.L.C.*, 526 F. App'x 381, 382–83 (5th Cir. 2013).

203. *Id.*

204. *Id.*

for McGlinchey to perform environmental due diligence.<sup>205</sup> To justify that holding, the court cited a letter from McGlinchey's expert stating that it was outside the scope of the firm's representation of Coves to investigate matters relating to real property unless counsel was "separately engaged" to do so.<sup>206</sup>

In further support of the contention that McGlinchey had no duty to exercise due diligence, the court noted that the record indicated Coves had already purchased the property before it had retained McGlinchey.<sup>207</sup> As such, McGlinchey did not represent Coves in connection with the purchase of the property.<sup>208</sup> Thus, the dicta in this case suggests that had McGlinchey been retained prior to the purchase of the property, it may have faced liability for breach of a duty to exercise environmental due diligence.<sup>209</sup>

*Keywell Corp. v. Piper & Marbury, L.L.P.* further illustrates the possibility of incurring liability for failure to exercise due diligence.<sup>210</sup> Keywell, a steel recycler, purchased a steel facility.<sup>211</sup> Its counsel, Piper & Marbury, hired an environmental consulting firm and worked in tandem to conduct an environmental due diligence audit.<sup>212</sup> Keywell, after incurring nearly \$6 million in environmental cleanup costs post-purchase, sued Piper & Marbury for malpractice and breach of fiduciary duty stemming from its alleged failure to provide an adequate environmental audit before the purchase.<sup>213</sup> Instead of arguing that it did not commit malpractice in its motion for summary judgment, the firm argued that Keywell could not prove damages from the alleged malpractice and breach of fiduciary duty.<sup>214</sup> The court ultimately denied the motion.<sup>215</sup>

Thus, the *Keywell* case supports the proposition that a failure to exercise due diligence—which could lead to damages to a client—can constitute a breach of fiduciary duty or a malpractice claim. Indeed, the court in *Keywell* noted that it is axiomatic that the relationship between the

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205. *Id.* at 384.

206. *Id.* at 385 n.2.

207. *Id.* at 384–85.

208. *Id.*

209. *See* Nolan, *supra* note 54, at 352 n.181.

210. *See* *Keywell Corp. v. Piper & Marbury, L.L.P.*, 96–CV–0660E(SC), 1999 WL 66700, at \*1 (W.D.N.Y. Feb. 11, 1999).

211. *Id.*

212. *Id.*

213. *Id.*

214. *Id.* at \*6.

215. *Id.* at \*11.

attorney and his client is fiduciary in nature.<sup>216</sup> The court further stated that “[a]s part of his or her fiduciary duty, the attorney must provide the client with all information material to the client’s decision to pursue a given course of action, or to abstain therefrom.”<sup>217</sup> Notably, the court did not consider the fact that Piper & Marbury followed certain customs in the industry, such as hiring an environmental consultant and reviewing that consultant’s audit, as dispositive in absolving it from liability.<sup>218</sup>

The above cases illustrate that lawyers may need to inform their clients of the effects of environmental hazards that stem from climate change in order to avoid future liability.<sup>219</sup> Analogous cases discussing the law of due diligence as it relates to risks other than environmental risks suggest the same.

### *B. The Standard of Care for Related Types of Due Diligence*

In *Spector v. Mermelstein*, the Second Circuit affirmed that an attorney’s malpractice in the form of negligent advising of a client was the proximate cause of the plaintiff’s damages.<sup>220</sup> The attorney failed to advise and discuss with his client material facts which would have caused the client to question the prudence of his decision to make a loan to another individual in financial distress.<sup>221</sup> In the original complaint, the plaintiff also alleged that his attorney had failed to exercise diligence in investigating and ascertaining the reputation and true financial condition of the individual to whom the client had given the loan.<sup>222</sup> In *Spector*, the attorney knew of the material facts before advising his client on how to proceed, and such knowledge made his failure to disclose more egregious than if the attorney had no such knowledge but could have acquired it through proper due diligence.<sup>223</sup> With respect to environmental due diligence, it is more likely that attorneys will not have complete knowledge of the risks before conducting any investigation, but the presence of this knowledge or lack thereof is not dispositive of the question as to whether the attorney exercised proper due diligence.

The related context of financial due diligence exemplifies the fact-intensive nature of the question of when attorney conduct falls below the

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216. *Id.* at \*4.

217. *Id.*

218. *Id.*

219. *See generally* MALLEY, *supra* note 193.

220. *Spector v. Mermelstein*, 485 F.2d 474, 483 (2d. Cir. 1993).

221. *See id.* at 480–81.

222. *See id.* at 477 n.3.

223. *See id.* at 480–81.

standard of care. Take for example federal securities law, which provides remedies to a purchaser of securities in a public offering when the purchase was made in reliance upon a disclosure document containing material misstatements or omissions.<sup>224</sup> The Securities Act of 1933 provides a cause of action against any underwriter of such securities; persons controlling the issuer or underwriter; sellers of the securities; and, in some cases, experts, including attorneys and accountants, with respect to the registration statement.<sup>225</sup>

Section 11(b)(3) of the Securities Act provides a due diligence defense to a person other than an issuer of the security.<sup>226</sup> To assert that defense, defendants must prove that: (1) after reasonable investigation; (2) they had reasonable grounds to believe that the statements in the registration statement were true; and (3) there was no omission of a material fact.<sup>227</sup> The appropriate standard of reasonableness for such investigation is that which “shall be that required of a prudent man in the management of his own property.”<sup>228</sup>

Courts’ interpretations of financial due diligence have described the standard of care as a “high bar.”<sup>229</sup> Those individuals who want to successfully assert this defense must demonstrate they did not simply rely on statements of company management when they could reasonably have examined documents or other materials relating to the matter in question.<sup>230</sup> For example, the seminal case *Escott v. BarChris Construction Corp.* held underwriters must independently verify all material facts in an issuer’s registration statement when independent verification is practicable.<sup>231</sup> It would be unreasonable to neglect to verify

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224. See 15 U.S.C. §§ 77k, 77l(a)(2).

225. *Id.* § 77k. A registration statement contains important information about its business operations, financial condition, results of operations, risk factors, and management. It must also include audited financial statements and is filed with the SEC. *What is a Registration Statement*, SEC, <https://www.sec.gov/small-business/goingpublic/registrationstatement> [<https://perma.cc/2UM7-TGCR>] (last visited Aug. 23, 2021).

226. 15 U.S.C. § 77k(b).

227. *Id.* § 77k(b)(3)(A).

228. *Id.* § 77k(c).

229. See 1 STEVEN C. ALBERTY, *ADVISING SMALL BUSINESSES* § 18:34 (2020 ed.), Westlaw ADVSB.

230. *Id.*

231. See Joseph K. Leahy, *The Irrepressible Myth of BarChris*, 37 DEL. J. CORP. L. REV. 411 (2012) (noting that *BarChris* is “universally understood to require that underwriters independently verify all material facts in the issuer’s registration statement if independent verification is practicable”); see *Escott v. BarChris Constr. Corp.*, 283 F. Supp. 643, 696 (S.D.N.Y. 1968).

material facts when one could easily do so.<sup>232</sup> Thus, the concept of due diligence, financial or otherwise, centers around the reasonableness of the inquiry that is the subject of the suit. Put another way, a familiar negligence standard of “knew or should have known” pervades the analysis of whether an individual has exercised adequate due diligence.

Insurance agents, when acting as fiduciaries, are also held to this type of reasonableness standard while exercising due diligence. For example, Ohio Revised Code section 3905.14 imposes a duty of due diligence upon insurance agents when selecting insurance coverage for their clients.<sup>233</sup> In the case *Workman v. Ohio Department of Insurance*, the Ohio Department of Insurance permanently revoked an agent’s insurance license after he failed to exercise due diligence in selecting appropriate providers of excess coverage for his clients.<sup>234</sup> The court noted the insurance agent owed a fiduciary duty to his customers to exercise good faith and reasonable diligence in seeking the coverage they needed.<sup>235</sup> The agent used a separate company to aid in the selection of relevant providers, and together they ultimately chose a provider that did not offer the requisite excess coverage.<sup>236</sup> Although the insurance agent’s expert claimed the agent conducted an investigation sufficient in the industry by using a separate company to select the coverage, the court held the agent did not exercise reasonable diligence, in part, because he did not make inquiries into whether the provider or the company he used were licensed to do business in Ohio.<sup>237</sup> Thus, the fact that the defendant followed industry practice did not absolve him of the duty he owed to the client.

It follows that a court may not absolve an attorney who does not diligently seek out flood-risk information of liability on the basis that it is not custom in the industry to seek out such information. Due to climate change-related flooding posing enormous risks, policy indicates that liability in such a case should not be so easily evaded.

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232. See *Escott v. BarChris Constr. Corp.*, 283 F. Supp. 643, 696 (S.D.N.Y. 1968).

233. OHIO REV. CODE ANN. § 3905.14 (2020).

234. See *Workman v. Ohio Dept. of Ins.*, No. 2012–CA–21, 2012 WL 4946298 (Ohio Ct. App. Oct. 17, 2012).

235. See *id.* at \*4.

236. See *id.*

237. See *id.*

*C. Failure to Relay Accurate Flood Risk Information: Negligence or Breach of a Fiduciary Duty*

The test to determine whether an attorney has conducted adequate environmental due diligence should follow the due diligence standards in other industries. Courts should assess the reasonableness of an investigation performed by an environmental attorney or other consultant on behalf of the client or produced for the client. The determination of reasonableness is a fact-specific, totality-of-the-circumstances approach. Further, facts associated with flood hazard must be gleaned from more than one source and should be independently verified where practicable.<sup>238</sup> This is already expected in general environmental due diligence. In such cases, parties exercise due diligence by checking for hazardous contamination liability under CERCLA. During their investigation, parties are expected to look to outside sources besides the EPA's list of contaminated or hazardous sites, as that list is not always comprehensive.<sup>239</sup> Further, a prudent attorney would want to consult with an environmental consultant that specializes in analyzing flood risk.

Scholars have recognized that, at the very least, *buyers* may be subjected by courts to a heightened standard of care for due diligence, noting that “notwithstanding the AAI rule, a judge or jury might still hold a ‘sophisticated buyer’ to a higher standard of due diligence than AAI.”<sup>240</sup> For example, a court may consider large corporations, as well as companies that routinely buy or sell commercial real estate, as “sophisticated.”<sup>241</sup>

As discussed, an investigation that goes beyond the NFIP flood maps is not the current standard of practice in the industry.<sup>242</sup> However, there are several reasons indicating that the cost-benefit analysis proposed in *The T.J. Hooper*—which determines whether following a standard of practice is unreasonable and therefore negligent—weighs in favor of a finding that an attorney may be negligent in only assessing flood risk as indicated by the problematic and inaccurate NFIP flood maps.<sup>243</sup>

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238. See Leahy, *supra* note 231, at 411.

239. See 30 C.F.R. § 312.27(c) (2019); see also Sadoski, *supra* note 143.

240. Vincent M. Gonzales et al., *Deal or No Deal: Recent Developments Impacting Environmental Due Diligence in M&A Transactions*, 25 No.5 ACC DOCKET 36, 42 (2007). It is unclear if the writer is discussing a CERCLA liability suit or a suit where a buyer sues a seller for rescission of the sale due to some condition of the property.

241. *Id.*

242. Karmel, Healy & Poplawski, *supra* note 13.

243. Jacobsen, *supra* note 33.

Indeed, courts have since cited *The T.J. Hooper* in their analyses regarding what the standard of care should be for certain professionals.<sup>244</sup> Courts have set the standard of care as higher than custom in the industry, holding that compliance with industry practice may be found to violate a standard of reasonable diligence.<sup>245</sup> For example, the Supreme Court of Washington has held that the precaution of administering a glaucoma test to patients under the age of 40 “is so imperative that irrespective of its disregard by the standards of the ophthalmology profession, it is the duty of the courts to say what is required to protect patients under 40 from the damaging results of glaucoma.”<sup>246</sup> Notably, the court held as much, notwithstanding the fact that the chance of a patient under the age of 40 contracting glaucoma is extremely low.<sup>247</sup> It follows then that if a court were presented with evidence that flood risk in a certain area was high, the court would consider it as further evidence that a failure to investigate flood risk was indicative of negligence.

The costs resulting from a failure to accurately assess the risks posed by climate change-related flooding could be quite large to the buyer. Thus, the benefit of an accurate analysis is also extremely significant. The Fourth National Climate Assessment conducted by the U.S. Global Research Program noted that rising sea levels, higher storm surges, and the ongoing increase in high tide flooding threaten public infrastructure and \$1 trillion in national wealth held by coastal real estate.<sup>248</sup> In addition, the discrepancies in the NFIP’s flood mapping system have historically been startling. For example, FEMA maps show that 0.3% of Chicago’s

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244. See, e.g., *S.E.C. v. EagleEye Asset Mgmt.*, 975 F. Supp. 2d 151, 160–61 (D. Mass. 2013) (denying a motion for summary judgment on a breach of fiduciary duty claim and stating that while the defendant “may assert that not discussing one’s track record is an industry practice, and while he may even point to the lack of a rule adopted by the SEC to require disclosing one’s track record, none of these declarations absolve him of his duty or ensure that he has satisfied that duty”).

245. See, e.g., *Tex. & Pac. Ry. Co. v. Behymer*, 189 U.S. 468, 470 (1903) (holding that a jury may find that compliance with industry practices violates a standard of “reasonable prudence”).

246. *Helling v. Carey*, 519 P.2d 981, 983 (Wash. 1974).

247. *Id.* at 982. Evidence of a low probability that a patient under 40 would contract glaucoma was presented as evidence that the custom in the industry was the correct standard of care, and therefore, the defendant was not negligent. However, the court noted that despite the low probability, the potential harm outweighed the risk of carrying out the precaution.

248. *Flood Insurance, Commercial Real Estate, and Climate Change*, JD SUPRA (Feb. 20, 2020), <https://www.jdsupra.com/legalnews/flood-insurance-commercial-real-estate-44260/> [<https://perma.cc/2P3A-WLKB>].

properties are within the 100-year flood zone.<sup>249</sup> However, when a third-party analytics company, First Street, reviewed the city of Chicago, they found about 13% of the city's properties were at risk.<sup>250</sup> This amounted to 75,000 more properties than depicted in the FEMA maps.<sup>251</sup>

Ensuring that the standard of care for environmental due diligence includes more accurate risk reporting by demanding information beyond the inaccurate NFIP flood mapping would be extremely beneficial. Demanding such information would result in more transparency in the actual amount of risks associated with a piece of property.<sup>252</sup> The financial sector has become increasingly focused on the importance of understanding climate change-related risks, such as physical flood risk to the asset itself as well as market-level risks associated with the surrounding real estate market of the asset.<sup>253</sup> These types of risks include the potential for the property to lose value or that local governments may not have adequate resilience strategies.<sup>254</sup> For example, the Task Force on Climate Related Financial Disclosures released a report to develop voluntary, climate-related disclosures of financial risk in financial filings for use by companies, banks, and investors in providing information to stakeholders.<sup>255</sup> This report essentially provided that the financial impact caused by climate change-related risks should be included in the financial filings of an organization.<sup>256</sup> The report underscores the importance of accurate information on climate change-related risks, noting that

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249. See Alex Broome, *Why Commercial Real Estate Owners Should Rethink Their Flood Risk*, RESHIELD (Aug. 24, 2020), <https://reshield.com/blog/why-commercial-real-estate-owners-should-rethink-their-flood-risk/> [<https://perma.cc/23GV-GCRT>].

250. *Id.*

251. *Id.*

252. Jacobsen, *supra* note 33.

253. URBAN LAND INSTITUTE & HEITMAN, CLIMATE RISK AND REAL ESTATE: EMERGING PRACTICES FOR MARKET ASSESSMENT 4 (2020) [hereinafter CLIMATE RISK AND REAL ESTATE], <https://knowledge.uli.org/en/Reports/Research%20Reports/2020/-/media/b81db4bbc77845f7834f24b0e974dd7a.ashx> [<https://perma.cc/NM93-9LP9>].

254. *Id.* at 1.

255. See TASK FORCE, *supra* note 157. Financial filings refer to annual reporting packages in which organizations are required to deliver their audited financial results under the corporate, compliance, or securities laws of the jurisdictions in which they operate. *Id.* at 62. These audited financial results are usually compiled during the due diligence process.

256. *Id.* at iii.

increasing transparency makes markets more efficient and economies more stable and resilient.<sup>257</sup>

In addition, investors are factoring in the level of flood risks, such as asset-level physical risks and market-level risks, into their decisions about making an investment.<sup>258</sup> Therefore, it is imperative that flood-risk due diligence be executed in a manner that uncovers the true nature of the risk. In yet another example of the importance of climate change-related risks, Moody's—a major credit agency that rates the creditworthiness of big borrowers, such as cities—accounts for the impact that climate change-related risks have on the government's ability to pay back the money they borrow by issuing bonds.<sup>259</sup> Moody's downgraded Cape Town, South Africa after three consecutive years of drought led to fears that the municipality would run out of water.<sup>260</sup>

On the other hand, one might argue that imposing a higher standard of care will increase the costs of real estate transactions.<sup>261</sup> Assessing the physical risks posed by climate change can be extraordinarily difficult.<sup>262</sup> While there are outside parties attempting to accurately predict flood risk, they have obviously not covered every area.<sup>263</sup> However, the private sector is developing more sophisticated tools to analyze climate change and its

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257. *Id.*

258. See CLIMATE RISK AND REAL ESTATE, *supra* note 253.

259. Kristoffer Tigue, *Climate Change Becomes an Issue for Ratings Agencies*, INSIDE CLIMATE NEWS (Aug. 5, 2019), <https://insideclimatenews.org/news/04082019/climate-change-ratings-agencies-financial-risk-cities-companies> [<https://perma.cc/6YJW-KHTD>]. Bond ratings, or credit ratings, much like individual credit scores, assess how likely it is that a borrower will repay debt. Those ratings can affect how much governments and companies are able to borrow and how much it will cost them. *Id.*

260. CLIMATE RISK AND REAL ESTATE, *supra* note 253, at 4.

261. See *Climate Change and Due Diligence: Impact on Real Estate Transactions*, THOMPSON HINE (Feb. 2, 2009), <https://www.thompsonhine.com/publications/climate-change-and-sustainable-business-solutions-update-climate-change-and-due-diligence-impact-on-real-estate-transactions> [<https://perma.cc/44NA-YZQR>].

262. See Annemargaret Connolly & Thomas D. Goslin, *Climate Change Considerations in M&A Transactions*, LEXISNEXIS (Nov. 4, 2019), <https://www.lexisnexis.com/practicalguidance/the-journal/b/pa/posts/climate-change-considerations-in-m-a-transactions> [<https://perma.cc/PC8G-GLU5>].

263. See generally FIRST ST. FOUND., <https://firststreet.org/> [<https://perma.cc/2YHL-WRBD>] (last visited Oct. 12, 2020).

subsequent environmental effects.<sup>264</sup> As such, leading investors are *already* piloting new practices in due diligence by analyzing flood risk associated with climate change.<sup>265</sup> Fitch Ratings and Four Twenty-Seven are third-party data analytics companies used by investors.<sup>266</sup> Data generated by these companies allows buyers, lenders, and investors to move away from strict reliance on FEMA flood maps and evaluate climate change concerns at a more forward-looking level.<sup>267</sup> Predictions indicate that ultimately the use of these companies will become standard practice in the industry.<sup>268</sup> In the meantime, however, the legal standard of care for environmental due diligence lags behind, providing no incentive for parties to utilize these cutting-edge technologies if they are not already inclined to do so and no disincentive for parties who deliberately wish to neglect them.

Another potential cost of increasing the standard of care is that the real estate market may experience a chilling effect. For example, Heitman, a real estate investment management firm, considered investing in an asset in a hurricane-prone area.<sup>269</sup> Heitman used the rating agency above, Fitch Ratings, to analyze the risks. Its analysis determined that acquiring this investment would cause the portfolio for which the asset was targeted to have an unacceptably high exposure to hurricane and flood risk.<sup>270</sup> Mary Ludgin, head of global research at Heitman, warned, “We now know our portfolio exposure to these climate-related risks. Over time, we want to lessen these risks. Our climate-risk assessment will not trigger an immediate sell-off of assets but it could (and has) caused us to opt not to buy assets with high exposure to environmental risks.”<sup>271</sup> This example illustrates there is ultimately a benefit in not investing in overly risky

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264. *Flood Insurance, Commercial Real Estate, and Climate Change*, JD SUPRA (Feb. 20, 2020), <https://www.jdsupra.com/legalnews/flood-insurance-commercial-real-estate-44260/> [<https://perma.cc/MW5Y-FK7R>].

265. URBAN LAND INSTITUTE & HEITMAN, CLIMATE RISK AND REAL ESTATE INVESTMENT DECISION MAKING (2019) [hereinafter HEITMAN], <http://www.heitman.com/wp-content/uploads/2019/02/ULI-Heitman-Climate-Risk-Report.pdf> [<https://perma.cc/E72W-B5KL>].

266. *See Flood Insurance, Commercial Real Estate, and Climate Change*, *supra* note 264; *see also Four Twenty Seven Receives Majority Investment from Moody's Corporation*, FOUR TWENTY-SEVEN (July 24, 2019), <http://427mt.com/2019/07/24/four-twenty-seven-receives-majority-investment-from-moodys-corporation/> [<https://perma.cc/X4JD-NDMB>].

267. HEITMAN, *supra* note 265, at 17.

268. CLIMATE RISK AND REAL ESTATE, *supra* note 253, at 6.

269. HEITMAN, *supra* note 265, at 17.

270. *Id.*

271. *Id.*

purchases. This is especially true given that flood mitigation in the form of “managed retreat” of flood-prone areas is growing increasingly likely.<sup>272</sup>

Opponents to any heightened standard of care may still assert that the costs of an accurate flood-risk analysis outweigh the benefits in smaller commercial real estate transactions in high-risk areas because it would be too costly to obtain the necessary tools to measure the risks. However, attorneys practicing environmental due diligence should at least be on notice that a failure to analyze flood risk might subject them to liability regardless of any supposed custom in their industry. Further, a court would likely consider the fact that an area is a well-known, high-risk area as evidence that a failure to analyze flood risk in that area constitutes negligence. Take, for example, the historic flood in August of 2016 in south Louisiana.<sup>273</sup> This flood was dubbed the “500-year flood event.”<sup>274</sup> However, most experts agree this does not mean such a flood is unlikely to occur again in the next 500 years.<sup>275</sup> Indeed, many homes and buildings outside high-risk flood zones were underwater after the 2016 flood.<sup>276</sup> Thus, an attorney who is familiar with and works in south Louisiana, and who does not wish to analyze flood risk may, at the very least, want to obtain a waiver of flood risk analysis from their clients. The waiver could notify clients that the property is a risk because of certain conditions in the area, reliance on FEMA flood maps is not adequate to determine flood risk, and the attorney is not certifying that the property is free from flood risk.

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272. See Flavelle et al., *supra* note 14.

273. See Steve Hardy et al., *What Caused the Historic August 2016 Flood, and What Are the Odds it Could Happen Again?*, THE ADVOCATE (Aug. 5, 2017), [https://www.theadvocate.com/louisiana\\_flood\\_2016/article\\_3b7578fc-77b0-11e7-9aab-f7c07d05efcb.html](https://www.theadvocate.com/louisiana_flood_2016/article_3b7578fc-77b0-11e7-9aab-f7c07d05efcb.html).

274. See *id.*

275. See *id.*

276. See MICHELLE ANNETTE MEYER ET AL., THE 2016 UNEXPECTED MID-STATE LOUISIANA FLOOD: WITH SPECIAL FOCUS ON THE DIFFERENT RESCUE AND RECOVERY RESPONSES IT ENGENDERED 276 (Shirley Laska ed., 2020), <https://link.springer.com/book/10.1007/978-3-030-27205-0> [https://perma.cc/29D2-9EEA]. It is important to note that, sometimes, residents will sue FEMA to have their properties removed from high-risk flood zones, often because these zones make insurance mandatory or more expensive. In fact, this is exactly what occurred in 2016. The author notes that residents of Central Louisiana won a case against FEMA to have about 2,000 homes removed from the high-risk flood zone, just before the catastrophic flooding. These homes were underwater after the 2016 flood. *Id.*

In sum, the benefits of seeking outside flood-risk information—either through third-party data analytics companies, flood experts, or consultants—outweigh the potential costs of solely relying on the NFIP’s inaccurate and outdated mapping system. These costs are substantial, not only for the actors consummating a transaction, but also for the commercial real estate market as a whole.

#### CONCLUSION

The standard of care required of professionals exercising environmental due diligence should include scrutiny of accurate data associated with the risk of flooding and its potential to increase due to climate change, which requires looking beyond the outdated NFIP maps.<sup>277</sup> Although the task of tackling climate change-risk is daunting, there is currently a phenomenon of “moral hazard”—a lack of incentive to guard against risk—that exists throughout the financial sector.<sup>278</sup> Incentivizing professionals to more accurately calculate risks before reporting to the buyer in a commercial real estate transaction will help to reduce this moral hazard and allow for more transparency in the market.<sup>279</sup>

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277. See discussion *supra* Part III.

278. See discussion *supra* Part III.

279. See discussion *supra* Part III.