# ENVIRONMENTAL CONCERNS

# FOR DEVELOPERS

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# Environmental Concerns for Developers

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## I. OVERVIEW OF ENVIROMENTAL REGULATION

The regulatory climate for development has changed markedly in the past decade. In addition to zoning and subdivision issues, the astute developer must analyze a multitude of environmental issues prior to reducing the project to a blueprint. As recently as five years ago, most development projects were shelved permanently if an initial investigation revealed existing environmental problems which potentially implicated liabilities under the far-reaching federal and state regulatory schemes. Financing for these projects could not be obtained, and no one, including the developer itself, was desirous of inheriting a project laden with potential environmental liabilities.

Times have changed at a pace that is remarkable in the regulatory field. The United States Environmental Protection Agency ("EPA") has itself recognized the impediment to development that the Superfund, or Comprehensive Environmental Response, Compensation, and Liability Act of 1980 ("CERCLA"), has imposed on innocent parties. Congress has finally vested lenders with a true "safe harbor," and the advent of brownfields legislation and guidance documents have encouraged, rather than frustrated, the development of environmentally blighted properties. In fact, the regulatory agencies have shifted their focus from an "all-out" remedial effort to a "risk based" response designed to assist developers in placing the property to its highest and best use.

This paper will review a common sense approach to developing an environmental baseline, which segregates existing environmental conditions from those which may develop after the closing of the purchase of the property. After discussion of the environmental

baseline, this paper will address the primary environmental permits necessary for a successful development, including air quality, hazardous waste, and wetlands issues. This presentation will then highlight the historical theories of liability and the limited defenses to environmental claims asserted under federal law, and compare that history to the recent judicial trend of expanding those defenses and thereby encouraging property development. Finally, the ability to "reuse" environmentally impaired properties will be discussed. The development of these impaired properties, commonly known as "brownfields," will be affected by the structure of the environmental baseline, the relief afforded to lenders providing the financing for the project, and by the recent judicial limitations on liability and the expansion of defenses available under federal law.

## II. ENVIRONMENTAL BASE LINE

In virtually every business development transaction, potential environmental liability is a risk that must be appropriately assessed. As the discussion of the Comprehensive Environmental Response, Compensation and Liability Act, 42 U.S.C. 9601 et. seq. ("CERCLA") in part V below indicates, liability is frequently based not as much on fault as on ability to pay. Additionally, future laws may impose potential construction or operational restrictions which may deprive a proposed project of economic viability. The role of the environmental attorney is to ensure that these risks are managed to achieve maximum value.

Environmental risks in buying or selling real estate can be segregated into the following four categories: (i) existing contamination of purchased property, which is largely governed by CERCLA; (ii) third-party claims which may be asserted by neighboring land owners; (iii) operational restrictions, including obtaining necessary environmental permits

and compliance with those permits; and (iv) enforcement actions, which may be instituted by an agency or an aggrieved citizen based on activities which preceded the purchase.

## A. Due Diligence

A properly conducted environmental review of a property or business should be designed to quantify known and perceived risks. Appropriate due diligence includes an identification of environmental conditions, a determination of whether those conditions must be remedied, the cost of any remedy, and the likelihood of third-party claims. These questions are initially answered by a Phase I Environmental Assessment, performed in accordance with the American Society for Testing of Materials ("ASTM") Phase I Standards. If a "Recognized Environmental Condition" potentially exists at the site, a Phase II Environmental Site Assessment may be warranted.

### 1. Sources of Due Diligence Information

a. Site History

1. Review of background information
2. In-house facility records review
3. Environmental records
4. Regulatory files
5. History of discharges
6. History of environmental citations
7. History of chemical material storage

b. Review of past operations on site

c. Review of state environmental records

d. Review of EPA records

e. Review of health records

f. Title search

g. Review of local tax assessor files

h. Site walk-through

1. Pre-walk through meeting with contact person to discuss current operations and past operations

2. Review on-site process operations

3. Review on-site materials

i. Review and observe environmental setting

j. Zoning

k. Proximity to residential areas

1. Proximity to water bodies

2. Proximity to wetlands

l. Physical inspection of all buildings and grounds (exterior and interior)

m. Review blueprints of the facility

n. Review storm sewers

o. Review leach fields

p. Review dry wells

q. Review process lines

r. Review sumps

s. Review floor drains

t. Review building vents

u. Review transformers

v. Physically trace handling of all hazardous materials and wastes to confirm any descriptions provided in records and operation manuals or narratives

w. Review possible migration pathways

x. Review all environmental permits

1. Determine nature and scope of permits

y. Review all site maps

z. Review all heating systems

aa. Review wastewater discharges

bb. Review hazardous substances

1. conduct waste inventory

2. check against company records

cc. Review all Material Safety Data Sheets ("MSDS")

dd. Review all OSHA requirements

ee. Review all hazardous substance containment facilities

1. note materials stored

2. note construction of storage containers

3. note storage units and include size, location and age

4. conduct necessary interviews with all operators and employees
5. conduct interviews with former employees and operators
6. consider Freedom of Information Act request to determine if there have been any alleged violations of any federal laws relating to hazardous materials or whether any enforcement actions have been brought against this owner or prior owners.

ff. Review all aerial photographs (if not immediately available, consult commercial sources)

1. Aerial photographs of most areas of the country are available for purchase commercially
2. Site photos are generally taken at ten-year intervals or less.

gg. Review all surrounding and neighboring uses

hh. Conduct appropriate physical and chemical screening tests

1. Direct read instrumentation (equipment that analyzes gas or vapor directly with the instrument displaying a measured value on a gauge)
2. Portable gas chromatograph: direction of soil vapors through chromatograph shows parameters to be separated and upon separation the target materials are measured using a sensor.
3. Metal detectors: confirm presence of underground tanks.
4. Field Test Kit: Detection of polychlorinated biphenyls

ii. Conduct, where appropriate, laboratory analysis of field samples

jj Analyze soils, sediments and sludges

a. Sample at or around underground tanks

b. Sample at or around piping areas

c. Physically collect samples

d. Laboratory analysis of collected samples

kk. Groundwater Analysis

a. Well installation

b. Sample collection

c. Laboratory analysis

**2. Representations and Warranties**

Common subjects for representations in connection with environmental matters include the following:

a. Compliance with laws and regulations;

b. Possession and effectiveness of required permits;

c. Lack of pending or threatened enforcement action; and

d. Lack of pending or threatened third-party claims.

Additionally, a buyer should require representations of the seller concerning the absence of undisclosed liabilities and whether hazardous substances have been used or stored on the property.

From the seller's perspective, an "AS IS" clause may not be sufficient to prevent the buyer from seeking reimbursement for environmental costs, as these types of clauses are generally construed against the seller. **Southland Corp. v. Ashland Oil Inc., 696 F. Supp. 994 (D.N.J. 1988)**.

**3. "As Is"**

Buyer agrees that, except as expressly set forth in this agreement, no representations by or on behalf of Seller have been made to Buyer as to the condition of the property, any restrictions related to the development of the property, the applicability of any governmental requirements, including, but not limited to "environmental requirements" pertaining to the property, or the suitability of the property for any purpose whatsoever. Buyer represents to Seller that Buyer has made its own independent investigation of the property and is relying solely on such independent investigation. Buyer acknowledges that Seller has no expertise concerning "environmental requirements" and "hazardous materials" and that Buyer is not relying on any representation or the lack of same, with respect to "environmental requirements" or "hazardous materials" as they apply to conditions on the property.

Through the environmental due diligence procedure, the parties are able to segregate pre-closing from post-closing liabilities. This segregation, commonly called the "Environmental Baseline," serves to establish responsibilities for environmental response costs and liabilities which are liquidated after the closing of the purchase and sale.

The following are examples of allocation and baseline provisions:

**4. Environmental Allocation**

Except as otherwise provided in this schedule, Seller shall be responsible for, and

bear the costs of, such corrective action as may arise as a consequence of the ownership or operation of the property prior to the closing date, and Buyer shall be responsible for, and bear the cost of, such corrective action as may arise as a consequence of the ownership or operation of the property on or after the closing date. The presence or absence or hazardous substances in the soil or groundwater on the property as of the closing date, for purposes of determining the necessity of corrective action, shall be conclusively determined by the baseline, as defined below.

**5. Environmental Baseline**

Except as otherwise provided, or specifically agreed to in writing, the presence or absence as of the closing date of hazardous substances in the soil or groundwater on the property, or that have migrated or may migrate from the property as a consequence of activities on or related to the property (hereinafter called the "Environmental Baseline"), shall be determined referenced to data from the environmental assessments performed by ABC Company. The Environmental Baseline shall not include the presence of substance in such quantities as are consistent with the method of operation of the property, in process equipment, storage tanks, land farm, or non-earth containment devices or of such substances as may lawfully exist as a consequence of the operation of the property ("lawful substances"). Buyer agrees to be responsible for any corrective action arising from the use of lawful substances after the closing date, and any contamination caused by those lawful substances after the closing date or related corrective action after the closing date.

## III. PRIMARY ENVIRONMENTAL PERMITS

### A. Air

#### 1. Construction Permit

Under the New Mexico Air Quality Control Act, **N.M. Stat. Ann. §§74-2-1 et. seq. (1978)**, the Environmental Improvement Board is designated as the state air pollution control agency. **N.M. Stat. Ann. § 74-2-3(B)** Section 74-2-7 requires an air quality permit for the construction or modification for the construction or "modification" of any new source. "Air pollution" is defined as

> "[t]he emission, except emission as occurs in nature, into the outdoor atmosphere of one or more air contaminants in such quantities and duration that may with reasonable probability injure human health, animal, or plant life or as may unreasonably interfere with the public welfare, visibility, or the reasonable use of property."

**N.M. Stat. Ann. § 74-2-2(B)(1978).**

#### 2. Regulation 702

Although often misunderstood by industry, Regulation 702 is not properly viewed as an operational permit. It addresses construction permits which are required before operation of an air pollutant "source" can occur. Consequently, environmental modeling studies must be completed well before construction, and must identify levels of potential emissions. Those emissions typically include Nitrous Oxide, Carbon Monoxide, and Non-Methane Hydrocarbons.

Part II of Regulation 702 provides that permits "must be obtained" from the Environment Department under the following circumstances: (i) prior to the construction of

a source which emits one or more regulated air contaminants for which there is a national ambient air quality standard or state ambient standard and which emits greater than ten pounds per hour of any regulated air contaminant or has a potential emission rate of greater than one hundred pounds per hour; and (ii) toxic air pollutants. Oil and gas operations, including distribution facilities, are exempt from the toxic air pollutant requirements. Consequently, the pertinent regulation is that which restricts emissions of certain designated constituents to ten pounds per hour.

Typically, the Environment Department will notify the applicant concerning the completeness of the permit application within thirty days after the application has been submitted. After notification of the completeness or lack thereof, the Environment Department is allowed one hundred twenty days to conclude the processing of the permitting application. Accordingly, an applicant may reasonably expect a one hundred-fifty day waiting period prior to the issuance of an air quality permit.

Many operators have concluded that a permit is not necessary if a catalytic converter or other device will reduce anticipated emissions below regulatory standards. The applicability of the permitting requirements is generally based on levels of uncontrolled "potential" emissions.

**B. Water**

The Federal Clean Water Act prohibits the discharge of pollutants by any person into navigable waters except in compliance with specified requirements of the Act. **33 U.S.C. §§1251 et. seq.**

1. Point Source Discharges

"Point Source" is defined in the Clean Water Act as "any discernable, confined and discrete conveyance, including but not limited to any pipe, ditch, channel, tunnel . . ." **33 U.S.C. § 1362(14)**. Point source discharges are prohibited unless authorized by a National Pollutant Discharge Elimination System Permit ("NPDES"). Traditionally, point source discharges have been deemed to be "discrete" discharges, from a source that is readily discernable. **See Hudson Riverkeeper Fund, Inc. v. Harbor at Hastings Associates, 917 F. Supp. 251, 257 (S.D.N.Y. 1996)**. However, the United States District Court for the District of Oregon recently held that cattle grazing constitutes a point source because the activity "may" result in water pollution. **See Oregon Natural Desert Ass'n v. Thomas**, **940 F.Supp 1534, 1541 (D.Or. 1996), overruled by Oregon Natural Desert Ass'n v. Bombeck, 172 F.3d 1092 (9th Cir. 1998)**. The difference between a "point source" and non-point source discharge is significant. All point source discharges are subject to the NPDES permitting program, whereas non-point source discharges generally are not so regulated.

The NPDES permitting program is the primary method by which pollutants can be added to waters of the United States in compliance with the Clean Water Act's discharge prohibition. NPDS permitting is accomplished pursuant to section 402 of the Act.

**C. Storm Water Permits**

The Clean Water Act has evolved to the point where NPDS permit requirements are imposed on storm water discharges. However, since the early 1990s, the EPA has established ten nation-wide permits available for developers. These nation-wide permits

require the filing of a Notice of Intent prior to construction and additional requirements concerning the observation and reporting of any pollutants which accumulate in storm water run-off.

**D. Wetlands Permit Section 404**

See Wetlands discussion in part IV below.

**E. Hazardous Waste Permitting**

**1. 42 U.S.C. § 6928(d)(1)**

Prohibited Act: Transport hazardous waste to a facility which does not have a permit.

**2. 42 U.S.C. § 6928(d)(2)**

Prohibited Act: Treat, store or dispose of any hazardous waste, without a permit, or in violation of a material condition of a permit, or in violation of any material condition of any interim status regulations or standards.

**3. 42 U.S.C. § 6928(d)(3)**

Prohibited Act: Omit material information or make any false material statement or representation for purposes of compliance with state or federal RCRA regulations.

**4. U.S.C. § 6928(d)(4)**

Prohibited Act: Generate, store, treat, transport, or dispose of, or otherwise handle any hazardous waste or destroy, conceal, or fail to file any required record.

5. **42 U.S.C. § 6928(d)(5)**

Prohibited Act: Transport any hazardous waste without a required manifest.

6. **42 U.S.C. § 6928(d)(6)**

Prohibited Act**:** Export a hazardous waste without the consent of the receiving country, or in a manner inconsistent with an international agreement.

## IV. WETLANDS REGULATION

The primary statutory provision regulating development in Wetlands is section 404 of the Clean Water Act ("CWA"), **33 U.S.C §1344**. The Clean Water Act prohibits the discharge of pollutants from discrete point sources into waters of the United States. **Id. § 1311(a)**. However, Congress authorized the Army Corp of Engineers under section 404 of the CWA to administer a separate permit program for discharges of dredged or fill material. This section has evolved into the federal government's primary tool to limit development in Wetlands.

Discharges of dredged and fill material have been defined so broadly that many development activities in jurisdictional Wetlands will involve a regulated discharge. The courts generally define "discharge of dredge material" as the addition of material excavated or dredged from waters of the United States, including run-off from a dredge material disposal area. **33 C.F.R. § 323.2(d)(1)**. In response to the settlement of civil citizens' suits which were critical of the Corp's regulations, the Corp adopted a strict view of regulating dredging operations.

Similarly, "discharge of fill material" is a broad category, covering almost every activity that involves earth moving or discharges into designated Wetlands. Among the regulated activities are "placement of fill that is necessary for the construction in a water of the United States; the building of any structure or impoundment requiring rock, sand, dirt or other material for a construction; site – development fills;" causeway or road fills; and many other protection devices. **33 C.F.R. § 323.2(f)(1997)**. Even the temporary stockpiling of soil from the construction of a drainage ditch or similar excavation may be a regulated discharge.

**A. Section 404 Permit Process**

In view of the expansive definition of dredging and discharging operations, all Phase I assessments should include a determination of whether the proposed development is in an area designated by the Corp as a Wetland. Maps maintained by the Corp and by the Fish and Wildlife Service may be found on EPA's Wetlands website: http:\\www.epa.gov\owow\wetlands\. Under the 1989 Interagency Federal Manual for Identifying and Delineating Jurisdictional Wetlands, three criteria must be present for an area to be considered a Jurisdiction Wetland: Wetland vegetation, hydric soils, and Wetland hydrology. The manual also provides that, in certain circumstances, the presence of one of the criteria may be presumed from the presence of the other two. If the proposed development is in a designated Wetland area, a section 404 permit must be obtained from the Corp of Engineers.

There are two types of section 404 permits - individual and general. The Corp issues general permits for categories of activities that involve only minimal environmental disruption. General permits may be issued on either a nation-wide or on a regional basis.

Consequently, it is necessary to investigate the applicable general permits and, if appropriate to redesign the project so it falls within the parameters of a general permit.

## V. CERCLA

### A. Background

Congress enacted the Comprehensive Environmental Response, Compensation and Liability Act ("CERCLA") in 1980, in an effort to control further damage to sites contaminated by hazardous substances. Ever since that time, the term "environmental liability" has taken on new meaning for American businesses. CERCLA is unusual - it imposes harsh concepts of liability on responsible and innocent parties alike, notwithstanding the fact that the environmental problems addressed by CERCLA have usually developed over long periods of time with involvement by numerous companies and individuals.

This part of the presentation addresses the historical concepts of liability under CERCLA, including liability traditionally imposed upon present owners of land, prior owners, successor owners of corporations, and lessees. After a discussion of the historical theories of liability, this paper addresses the recent expansion of the previously limited defenses available to potentially responsible parties. Finally, this presentation addresses contribution rights among parties who are potentially liable under CERCLA, and Congress's recent efforts to limit the scope of CERCLA liability for lenders.

### B. Historical Theories of Liability

#### 1. CERCLA Imposes Broad Liability

In the event that hazardous substances have been "released" from "a facility," **see 42**

**U.S.C. § 9601(22)**, four groups of defendants may be liable for environmental response costs incurred by the government or by a private party plaintiff. The breadth of liability has not been limited to those who are culpable, in one way or another, for the environmental degradation. The group of defendants includes: (i) the current owner, whose only mistake may have been to purchase the property, and the current operator; (ii) past owners and operators at any time during which the disposal of hazardous substances occurred; (iii) persons who arranged for disposal of those substances; and (iv) the transporters who selected the ultimate disposal site. **See 42 U.S.C. § 9607(a)**. There is no necessity under CERCLA for a private party plaintiff or the government to show that any of the four potential groups of defendants was negligent or wrongfully conducted activities at the site. On the contrary, CERCLA imposes strict liability, **United States v. Davis, 261 F.3d 7, 28 (1st Cir. 2001)** and the lawfulness of the previous activities at the site is irrelevant to the imposition of that liability, **see State of New York v. Shore Realty Corp., 759 F.2d 1032, 1043-1044 (2nd Cir. 1985).**

In addition to the abandonment of culpability under CERCLA, any and all of the four potential groups of defendants have traditionally been jointly and strictly liable for indivisible pollution. **See, e.g., Sun Co., Inc. v. Browning-Ferris, Inc., 124 F.3d 1187, 1189 (10th Cir. 1997);United States v. Chem-Dyne, 572 F. Supp. 802, 805-10 (S.D. Ohio 1983).** Accordingly, it has been the defendant's burden to prove that her individual contamination may be sufficiently segregated and apportioned for purposes of liability. Given the complexities of groundwater management and the somewhat theoretical nature of hydrology, one can easily conclude that this burden is extremely difficult, if not impossible,

to establish at trial. This problem is exacerbated by the fact that the plaintiff need not prove that there is a causal link between the hazardous substances deposited by the defendant and the hazardous substances which have actually caused damage to the environment. **See, e.g., Chem-Dyne, 572 F. Supp. 802 (S.D. Ohio 1983). But see recent developments discussed in paragraph V H3 below.**

In the early 1990s, the Second and Third Circuits addressed the question of divisibility of harm. In separate cases involving the same parties, both Courts adopted the position that a defendant may escape liability if it can show that "its pollutants, when mixed with other hazardous wastes, did not contribute to the release or the resulting response costs." **United States v. Alcan Aluminum Corp., 990 F.2d 711, 717 (2nd Cir. 1993); see United States v. Alcan Aluminum Corp., 964 F.2d 252 (3rd Cir. 1992).** This determination will depend on the facts of each case, but it remains the defendant's burden to show divisibility. **U.S. v. Alcan, 964 F.2d at 269.**

Yet another approach to the division of joint and several liability was adopted in **United States v. A & F Materials Co., Inc., 578 F. Supp 1249 (S.D. Ill. 1984)**. There the Court looked to whether there is a reasonable basis on which to apportion liability. If it finds none, the Court may nonetheless decline to impose joint and several liability if the result would be inequitable. **See In the Matter of Bell Petroleum Services, Inc., 3 F.3d 889 (5th Cir. 1993)** (discussion of the evolving approaches to joint and several liability). Whether the harm suffered by the plaintiff is apportionable is a question of law. **Id. at 902.**

### C. Theories of Liability Against Present and Prior Owners

#### 3. Present Owner Liability.

42 U.S.C. § 9607(a) provides that persons liable under CERCLA include: "(1) The owner . . . of . . . a facility . . . ." Thus, probably the most appropriate way to define the theory of liability against a present owner of property is that of a "status tort." **See Moskowitz, Environmental Liability and Real Property Transactions, 48 (1989).**

The imposition of absolute liability on present, innocent owners is somewhat ironic, particularly considering the expressed intent of Congress in enacting CERCLA. CERCLA was enacted because "Congress intended that those responsible for problems caused by the disposal of chemical poisons bear the costs and responsibility for remedying the harmful conditions they created." **United States v. Reilly Tar & Chem. Corp., 546 F. Supp. 1100, 1112 (D. Minn. 1982).** According to one author and a variety of courts, the theme of CERCLA was "the imposition of liability for the effects of past disposal practices . . . on those who created and profited from waste disposal - generators, transporters, and disposal site owner/operators." **See Moskowitz, supra at 49; United States v. Northeastern Pharmaceutical & Chemical Company, 579 F. Supp. 823, 840 (W.D. Mo. 1984)** ("Congress intended to have the chemical industry, past and present, pay for the costs of cleaning up inactive hazardous waste sites."). **See, also, United States v. Bliss, 667 F. Supp. 1298, 1304 (E.D. Mo. 1987); overruled on other grounds by U.S. v. Davis, 794 F.Supp. 67 (D.R.I. 1992); United States v. Price, 577 F. Supp. 1103, 1114 (D.N.J. 1983).**

Where does this leave the person who is not a chemical manufacturer and who

purchased the site without knowing that it had previously been used for disposal activities? The so-called "polluter pays" policy simply has no application in this situation. Thus, it has been suggested that in 1980, Congress mistakenly attached absolute liability to innocent owners by a drafting error. By 1986, however, due to the increased costs associated with remediation, no one had seriously questioned the liability of the innocent, present owner. **See Moskowitz, supra, at 49.** This liability was solidified by the Superfund Amendments and Reauthorization Act of 1986, Pub. L. No. 99-499, 100 Stat. 1613 (1986) ("SARA"), which states that the liability of present owners includes those who acquired "title or possession" through "land contracts, deeds or other instruments." **42 U.S.C. § 9601(35)**.

The theories of liability against present owners have mushroomed. The definition of "owner" has been extended by one Court to include a lessee or a sublessor. **See United States v. South Carolina Recycling & Disposal, Inc., 653 F. Supp. 984 (D.S.C. 1984).** Another Court conferred ownership status on a beneficiary of a trust who, by definition, did not possess any indicia of legal ownership. **See United States v. Burns, 1988 WL 242553 (D.N.H. 1988).**

**2. Prior Owner Liability.**

Prior owners of a site are liable under 42 U.S.C.A. § 9607(a)(2), which states as follows:

> [A]ny person who at the time of disposal of any hazardous substance owned . . . any facility at which such hazardous wastes were disposed of . . .

**42 U.S.C. § 9607(a)(2).**

While some authors have suggested that current theory imposes liability on anyone in the "chain of title" of a particular property, the precise language of Section 9607 (a)(2) is to the contrary. **See Moskowitz, supra, at 50.** The literal interpretation of the section appears to require a finding of ownership during the time of disposal before liability can attach. Consequently, before the enactment of SARA in 1986, it was possible for an owner of a property to avoid liability simply by transferring title. SARA expressly closed this loophole by providing the following in 42 U.S.C. § 9601 (35)(C):

> [I]f the defendant obtained actual knowledge of the release or threatened release of a hazardous substance at such facility when the defendant owned the real property and then subsequently transferred ownership of the property to another person without disclosing such knowledge, such defendant shall be treated as liable . . . and no defense . . . shall be available to such defendant.

**42 U.S.C. § 9601(35)(c)** (emphasis added).

It therefore appears that the following types of prior owners may avoid liability: (i) those without knowledge of the contamination; and (ii) prior owners with knowledge who conveyed the property with adequate disclosures. However, a significant barrier exists in order to employ the escape route provided by 42 U.S.C. § 9601(35)(C). If there has been a "disposal" during your client's period of prior ownership, the exception of 42 U.S.C. § 9607(a)(2) is unavailable. **See United States v. Price, 523 F. Supp. 1055 (D.N.J. 1981), aff'd, 688 F.2d 204 (3d Cir. 1982)** ("disposal" includes continued leaking during the period of ownership); **Tanglewood East Homeowners v. Charles-Thomas, Inc., 849 F.2d 1568 (5th Cir. 1988)** (grating of property constitutes disposal).

With respect to prior owners, one author has suggested that the best reading of CERCLA is that a prior owner has no liability and therefore no need for a defense if (i) she purchased the property after the release was completed and (ii) she either (a) sold the property with ignorance of the release or (b) disclosed the release to the purchaser. **42 U.S.C. § 9607(a)(2)**. **See Moskowitz, supra, at 53.**

**D. Traditional Defenses Available Under CERCLA**

**1. Third-Party Defense – Present Owners.**

An innocent purchaser may avoid liability if he can establish that the release or threat of release was caused solely by:

> An act or omission of a third party other than an employee or agent of the defendant, or than one whose act or omission occurs in connection with a contractual relationship, existing directly or indirectly, with the defendant . . .

**See 42 U.S.C. § 9607(b)(3)** (emphasis added). Innocent owners have been plagued by the inarticulate drafting of the "third-party" defense. The "third-party" defense is not available if (i) the release occurred "in connection with a contractual relationship, existing directly or indirectly, with the defendant," or (ii) if no contractual relationship existed and the release was not solely caused by another. **Id**. It is difficult to determine precisely what this means. Under SARA, the term "contractual relationship," for the purpose of § 9607(b)(3), includes "land contracts, deeds or other instruments transferring title or possession . . ." **See 42 U.S.C. § 9601(35)(A); see also, United States v. Monsanto Co., 858 F.2d 160, 169 (4th Cir. 1988).** Arguably, every present owner has a contractual relationship, in some way or

another, with a previous polluter in her chain of title.

It is absurd to suggest that a deed or lease or any other "contractual relationship" transferring possession explains how any pollution caused by a predecessor was done "in connection with" a contractual relationship. Nonetheless, Courts have used the mere existence of a contractual relationship, wholly divorced from any connection with the activities of the polluter, to impose liability on a subsequent owner. **See, e.g., United States of America v. Monsanto Co., 855 F.2d 160, 169 (4th Cir. 1988).**

**4. SARA "Due Diligence" Defense.**

Because of the implausibility of the third-party defense and the broad nature of "a contractual relationship" with a previous polluter, SARA has provided some minimal relief in the form of the due diligence defense. Thus, there is an exception to liability through the "contractual relationship" where:

> [T]he real property on which the facility concerned is located was acquired by the defendant after the disposal or placement of the hazardous substance on, in, or at the facility, and . . .
>
> (i) At the time the defendant acquired the facility the defendant did not know and had no reason to know that any hazardous substance which is the subject of the release or threatened release was disposed of, on, in or at the facility.

**42 U.S.C. § 9601(35)(A)**. This language therefore requires complete innocence on the part of the new owner. A new owner must not have caused the pollution, he must not have been there when it was caused, and he must not know about it when the property was acquired. Plainly, the drafters of CERCLA attempted to promote so-called "due diligence" investigations prior to the acquisition of property. **See United States v. Pacific Hidet Fur**

**_____, 716 F. Supp. 1341 (D. Idaho 1989)** (defense available); **O'Neil v. Picillo, 682 F.Supp. 706 (D.R.I. 1988) aff'd., 883 F.2d 176 (1st Cir. 1989)** (defense not available - release not caused "solely" by a third party); **United States v. Hooker Chem. & Plastics Corp., 680 F. Supp. 546 (W.D.N.Y. 1988)** (third party defense not available); **United States v. Serafini, 706 F. Supp. 346 (M.D.Pa. 1988)** (question of fact precluding summary judgment as to customary practice in acquiring contaminated site in 1969); **State of Washington v. Time Oil Co., 687 F. Supp. 529 (W.D. Wash. 1988)** (innocent landowner defense rejected where company failed to show that it exercised due care with respect to hazardous substances on property); **United States v. Mottolo, 695 F. Supp. 615 (D.N.H. 1988)** (due diligence defense not available where third parties were not the sole cause of contamination).

**5. No Recovery of Costs for Actions Inconsistent with the National Contingency Plan.**

Defendants may also escape liability for recovery of any cost incurred by the government which is inconsistent with the National Contingency Plan. The burden is on the defendant to show the government's chosen response action was inconsistent with the Plan and that the government acted arbitrarily and capriciously in choosing that response action. **U.S. v. Hardage Steering Committee, 982 F.2d 1436, 1442 (10th Cir. 1992) cert. denied, 510 U.S. 913 (1993); see also U.S. v. Northeastern Pharmaceutical & Chemical Co., Inc., 810 F.2d 726 (8th Cir. 1986) cert. denied, 484 U.S. 848 (1987).** An excessive cost can be challenged if the defendant argues that the government arbitrarily and capriciously failed to consider cost as a factor when deciding on the appropriate response, or selected a response

action that was not cost-effective. **Hardage, 982 F.2d at 1443**.

**4. Contribution no more than Background Contamination.**

The Second Circuit, in **United States v. Alcan Aluminum Corp., 990 F.2d 711 (2nd Cir. 1993)**, denied the government's motion for summary judgment and allowed Alcan to argue that it should have no liability for clean-up costs if it could show that its oil emulsion, when mixed with other wastes, did not contribute to the releases at the site or to the clean-up costs. Alcan suggested that its oil emulsion waste contributed no hazardous substances to the site. While allowing the argument, the Court put the burden of proof on the defendant. The decision in **Alcan Aluminum Corp.** was one of the first to recognize a limited exception to the no causation or strict liability rule where EPA thresholds for a pollutant are absent.

**E. Summary Liabilities and Defenses**

**1. Prior Owners.**

A prior owner should not need a defense under CERCLA if the statute imposes no liability. Thus, if the prior owner had not performed adequate due diligence, the only consequence should be the unavailability of the "innocent purchaser" defense. **See Moskowitz, supra, at 53**. But if the prior owner did not own the property during the time of disposal, no liability should attach under the express language of 42 U.S.C. § 9607 (a) (2). Thus, it appears that CERCLA and the SARA amendments should not impose liability upon prior owners if the prior owner purchased the property after the release and subsequently sold the property (i) without knowledge of any release or (ii) after disclosing the release to the purchaser.

**2. Present Owners**

With respect to present owners, CERCLA provides little, if any, relief. To avoid liability, present owners must establish that the pollution was caused solely by the actions of other parties and that the release either (i) did not occur in connection with a contractual relationship (the third-party defense, which has traditionally been meaningless); or (ii) the release occurred in connection with a contractual relationship, but the elements of the due diligence defense have been satisfied.

**3. Successor Liability.**

The general rule is that merging a liable corporation with another corporation is an ineffective means to avoid the transfer of liability. In such a situation, the liability simply follows the corporation, regardless of the identity of the new owner or its shares. **Id. at 91**. On the other hand, it may be possible to acquire the assets of a corporation without acquiring unrelated liabilities. **See Smith Land & Improvement Corp. v. Celotex Corp., 851 F.2d 86, 91 (3rd Cir. 1988) cert. Denied, 488 U.S. 1029 (1989). But see Ortiz v. South Bend Lathe, 46 Cal. App. 3d 842, 846, 120 Cal. Rptr. 556 (1975)** (transfer of contaminated asset results in liability for owner.) **See also Moskowitz, supra, at 99-100.**

**4. Lessee Liability.**

CERCLA is not clear on the issue of lessee liability, since the statute is phrased in terms of "operators." 42 U.S.C. § 9607 establishes liability for:

(1) the . . . operator of a facility,

(2) any person who at the time of disposal of any hazardous substance . . .

Although liability for an active operator is clear, the section does not clearly define liability for a passive lessee. **See** discussion of the "due diligence" defense, **supra**. Again, Section 9607(b)(3) creates a defense if the release was caused solely by the act or omission of a third party, but the defense is not available if the release occurred in "connection with a contractual relationship." The term "contractual relationship," under section 9601(35)(A) includes "other instruments transferring title or possession . . . A lease generally transfers possession.

Arguably, therefore, a passive lessee may be required to establish the elements of a "due diligence defense," the same as required for a present owner. This defense would require proof that the transfer of possession occurred after disposal of the waste and the lessee had no reason to know of the disposal. **42 U.S.C. § 9601(35)(A)**. **See also Rodburg, Landlord and Tenants in the Age of Environment, 3 Natural Resources & Environment, 10, 14 (Fall 1988). See also Moskowitz, supra, at 74-75.**

**5. Arranger Liability**

Section 107(a)(3) of CERCLA imposes liability upon persons who arrange for the disposal of hazardous substances that they own or possess. Presumably, the intent of this section is to impose liabilities on the "generators" of hazardous substances, notwithstanding the fact that they may not own the land upon which the hazardous substances are ultimately deposited. These persons are in the best position to control the disposition of hazardous substances and arguably to avoid the effects of allowing these substances to be released into the environment.

### 6. Liability for Persons who Accept Hazardous Substances for Transportation

Section 107(A)(4) of CERCLA imposes liability upon transporters. This liability provision is somewhat limited, as it applies only to those carriers who selected the destination for disposal of hazardous substances. Consequently, if the transporter transports the substances to a disposal site selected by the generator, the transporter does not incur liability. **42 U.S.C. § 9607(a)(4)**.

## F. Scope of Liability

Under Section 107, a liable party is responsible for the following:

(a) All costs of removal or remedial action incurred by the United States or a state which are "not consistent with the national contingency plan ("NCP");

(b) Any other necessary costs of responses incurred by any other person "consistent" with the NCP; and

(c) Damages for injury to, destruction of, or loss of natural resources, including the reasonable costs of assessing such injury, destruction or loss.

Note the difference between (a) and (b) above. In an action initiated by the EPA or by the State, the defendant has the burden to prove that the costs incurred by the EPA or by the State were "inconsistent" with the NCP. **See United States v. Northeastern Pharmaceutical & Chem. Co., 810 F.2d 726 (8th Cir. 1986) cert. Denied, 484 U.S. 848 (1987).** In a private party cost recovery action, the plaintiff must prove, under (b) above, that the necessary costs of response were "consistent" with the NCP.[2] **See City of New York v.**

**_____, 633 F. Supp. 609 (S.D.N.Y. 1986).**

**G. Private Party Litigation**

**1. Right of Contribution**

Although the early decisions addressing private party contribution rights held that such a right existed under federal common law, **see United States v. Ward, 1984 WL 15710 (E.D.N.C. 1984)**, the language of section 107 seemingly makes such a common law analysis unnecessary. Section 107 provides that covered parties are liable for costs "incurred by any other person." **42 U.S.C. Section 9607(a)(4)(A). See City of Philadelphia v. Stepan Chem. Co., 544 F. Supp 1135, 1141-43 (E.D. Pa. 1982).** The 1986 SARA amendments, however, resolved any confusion on this issue. **42 U.S.C. § 9613(f)(1)** provides that "[a]ny person may seek contribution from any other person who is liable or potentially liable under section 9607(a)."

In the early years of CERCLA, some Courts held that a private party may recover costs from another only if the site was listed on the National Priority List. **See Cadillac Fairview v. Dow Chemical Company, 1984 WL 178617 (C.D. Cal. 1984)**. Other Courts expressed the more rational view that only some form of government approval is necessary before allowing a private party cost recovery action. **See Bulk Distributing Centers, Inc. v. Monsanto Co., 589 F. Supp. 1437 (S.D. Fla. 1984); Pinole Point Properties Inc. v. Bethlehem Steel Corp., 596 F. Supp. 283 (N.D. Cal. 1984).** The better view, however, appears only to require private parties to prove that the costs incurred were "consistent with" the NCP. **United States v. Northeastern Pharmaceutical & Chem. Co., 579 F. Supp. 823 (W.D. Mo. 1984); Amoco Oil Co., v. Borden, Inc., 889 F.2d 664 (5th Cir. 1989);**

**Cadillac Fairview/California v. Dow Chemical Co., 840 F.2d 691 (9th Cir. 1988); Tanglewood East Homeowners v. Charles-Thomas, Inc., 849 F.2d 1568 (5th Cir. 1988); Roe v. Wert, 706 F. Supp. 788 (W.D. Okla. 1989)** (citizen suit requires 60-day pre-suit notice); **Wickland Oil Terminals v. Asarco, Inc., 792 F.2d 887, 890 (9th Cir. 1986); NL Industries, Inc. v. Kaplan, 792 F.2d 896 (9th Cir. 1986).**

**2. Extent of Contribution**

In apportioning liability among private parties for response costs, the Courts may consider a broad range of equitable factors under section 113(f). These factors are set forth in the legislative history of the amendment, and they include (i) the amount of the hazardous substances involved; (ii) the toxicity level of the hazardous substances; (iii) the degree of the parties' involvement in disposing of the hazardous substances; (iv) the level of care exercised; and (v) the degree of the parties' cooperation with federal, state or local officials. **See H. Rep. No. 153, 99 Cong., 1st Sess. 18-19 (1985).**

Because a present owner of a facility is a person who may be liable for response costs under section 107, the issue of contribution often arises where the present owner, who arguably had nothing to do with the disposal of the contaminants, brings suit under CERCLA against the generators and transporters of the hazardous substances. In **Gopher Oil Co. v. Union Oil Company of California, 757 F. Supp. 988 (D. Minn. 1990)**, the Court allocated all of the liability for past and future response costs to the previous site owner. In **Gopher**, the present owner neither caused nor contributed to the contamination of the property. In **Weyerhauser Co. v. Koppers Co., 771 F. Supp. 1420 (D. Md. 1991),** the Court reached a different result on markedly different facts. The owner in **Weyerhauser** not only knew of

and acquiesced in the disposal activities, but also had required them as a condition of the lease with the operator. Consequently, the Court reasoned that the owner had received some benefit from the operations, and apportioned the liability 40% to the owner and 60% to the operator. **See, e.g., United States v. A&F Materials Co., 578 F. Supp. at 1256; Amoco Oil Co. v. Borden, Inc., 889 F.2d at 672-73; United States v. Monsanto, 858 F.2d at 168 n.13.**

**3. Conditions Precedent to Private Action.**

Before initiating a claim under CERCLA, the party seeking cost reimbursement must have incurred at least one cognizable response cost. **See Trimble v. Asarco, 232 F.3d 946, 951 (8th Cir. 2000); Cook v. Rockwell International Corp., 755 F. Supp. 1468 (D. Colo. 1991). See also Alloy Briquetting Corp. v. Niagara Vest, Inc., 756 F. Supp. 713 (W.D.N.Y. 1991).**

**4. Attorney's Fees.**

The Supreme Court has addressed the question of whether attorney's fees are a "necessary cost of response" within the meaning of CERCLA § 107 (a) (4) (B) to resolve a dispute between the Circuits. **Key Tronic Corporation v. United States, 511 U.S. 809 (1994)**. Key Tronic brought suit against the Air Force for contribution of clean-up costs, including attorney's fees. The Court found no clear congressional intent to overcome the presumption that each party must pay its own costs in a recovery action. The Court distinguished between costs incurred in pursuing litigation in one party's interest, and those actions which relate directly to actual clean-up. The cost of identifying other responsible parties may be a reimbursable necessary response cost, even if the work is done by an

attorney. **FMC Corp. v. Aero Industries, Inc., 998 F.2d 842 (10th Cir. 1993).**

### H. Approaching the Third Decade of CERCLA

In the 1980s and early 1990s, the federal Courts generally rejected all arguments against broad liability under CERCLA. As CERCLA enters its third decade, new trends can be gleaned from the judicial decisions. These trends are exemplified in a recent Supreme Court decision defining the breath of liability under Section 107, decisions narrowing liability from the passive migration of contaminants, and judicial efforts to resurrect the third-party defense under Section 107(b)(3).

#### 1. Corporate Liability

In 1991, the United States District Court for the Western District of Michigan held that a corporate parent could be liable under CERCLA for contamination at a site owned and operated by a subsidiary. **See CPC International, Inc. v. Aerojet-General Corp., 777 F. Supp. 549 (W.D. Mich. 1991).** Focusing on the remedial nature of the statute instead of on the traditional corporate doctrine of limited liability, the District Court held that if a corporate parent exercises "power" or influence over its subsidiary by actively participating and exercising control over the subsidiary's business during a period of disposal of hazardous wastes, then the parent is directly liable under CERCLA. **Id. at 573**. After a decision by the Sixth Circuit, the Supreme Court granted certiorari to clarify the issue of corporate parent liability under CERCLA. **United States v. Bestfoods, 524 U.S. 51 (1998).**

In **Bestfoods**, the Supreme Court reverted to traditional notions of corporate limited liability by holding that a parent corporation that actively participates in and exercises

control over the operations of a subsidiary may not be held liable as an operator of a contaminated site owned and operated by the subsidiary, unless the corporate veil is pierced under state law. The Supreme Court expressly found that CERCLA does not authorize a departure from traditional principles of limited liability for a corporate parent: "It is a general principle of corporate law deeply 'engrained in our economic and legal systems' that a parent corporation (so-called because of control through ownership of another corporation's stock) is not liable for the acts of its subsidiaries. . . . Although this respect for corporate distinctions when the subsidiary is a polluter has been severely criticized in the literature, . . . nothing in CERCLA purports to reject this bedrock principal, and against this venerable common law backdrop, the congressional silence is audible." **Id. at 1884-85.**

It is important to note that, in **Bestfoods**, the Supreme Court recognized that a parent corporation may be liable directly for its own acts where those acts satisfy the elements of operator liability under CERCLA. **Id. at 1886.** However, the Court refused to sanction a broad interpretation of the statute which would place (i) direct CERCLA liability on a parent under circumstances where the parent is not a "operator" based on its own actions or (ii) vicarious liability under circumstances where the corporate veil could not be pierced by traditional veil–piercing standards. **Id. at 1885-87.** The Court refused to discard the notion that officers employed by both the parent and a subsidiary are presumed to serve the subsidiary when acting on behalf on the subsidiary. The Court explained "there would in essence a relaxed, CERCLA–specific rule of derivative liability that would banish traditional standards and expectations from the law of CERCLA liability." **Id.**

**2. Passive Migration**

In the late 1980s and the early 1990s, the majority of Courts that addressed this issue viewed passive migration of contaminants as a form of disposal under CERCLA. **See, e.g., Nurad, Inc. v. William E. Hooper and Sons, 966 F.2d 837, 845 (4th Cir.), cert. denied, 506 US 940 (1992); Stanley Works v. Snydergeneral Corp., 781 F. Supp. 659, 664 (E.D. Cal. 1990).** In **Nurad Inc.**, the Fourth Circuit reasoned that reading "disposal" to require "active participation" would frustrate CERCLA's policy to remedy environmental hazards. **Nurad, 966 F.2d at 845.**

The more recent decisions have retreated from such a broad reading of "disposal." Under current decisions, passive migration of contamination does not invoke CERCLA liability unless a party consciously acted to dispose of the waste or acted in a manner that promoted migration. **See, e.g., United States v. 150 Acres of Land, 204 F.3d 698, 704 (6th Cir. 2000);ABB Industrial Sys., Inc. v. Prime Tech, Inc., 120 F.3d 351, 358-59 (2nd Cir. 1997)**; **United States v. CDMG Realty Co., 96 F.3d 706, 713 (3d Cir. 1996); Kalamazoo River Study Group v. Rockwell Int.l, 3 F. Supp. 2d 799, 812 (W.D. Mich. 1998); Carson Harvard Village Ltd., v. Unocal Corp., 990 F. Supp. 1188 (C.D. Cal. 1997).**

In **ABB Industrial**, the Second Circuit held that prior owners and operators of a contaminated site were not responsible under CERCLA for the passive migration of chemicals that were already in the ground. In **CDMG Realty,** the Second Circuit determined that CERCLA's definition of "disposal" was not so broad as to hold a prior owner or operator liable for the passive migration of contaminants from a landfill. **CDMG Realty, 96 F.3d at 714.** The Court stated that rejecting liability for passive migration is consistent with CERCLA's goal to "force polluters to pay the costs associated with their

pollution." That goal is not served if "a person [who] merely controlled a site on which hazardous chemicals have spread without that person's fault is liable as a polluter." **ABB Industrial, 120 F.3d at 358-59. See, also M. Chertok and M. Bogin, "Passive Disposal: New Protection Now Available" 218 N.Y.L.J. S2 (1997).**

### 3. Resurrection of the Third-Party Defense

Traditionally, the Courts have rejected a third-party defense for contaminants that were released during the period of the defendant's ownership of the site. In such a situation, the Courts generally concluded that, although the owner was not directly responsible for the tenant's actions, the release was not caused "solely by the acts or omissions of a third-party," and the defendant failed to take precautions against the foreseeable acts of others. **See**, **e.g.**, **New York v. Shore Realty Corp., 759 F.2d 1032 (1985)**.

In the mid and late 1990s, the Courts have been more receptive to the third-party defense. In **New York v. Lashins Arcade Co., 91 F.3d 353 (2nd Cir. 1996)**, the Second Circuit held that a shopping center owner was not liable under CERCLA for contamination from a dry cleaner that leased space years before the site owner had acquired the property. The Second Circuit held that the shopping center owner was protected by the third-party defense. In **Lashins Arcade Co.,** the State of New York argued that the shopping center owner was not entitled to the third-party defense because it had failed to adequately investigate the site, or to exercise "due care" regarding the contamination which existed. The Second Circuit rejected the State's arguments:

> It is surely the policy of CERCLA to impose liability upon parties responsible for pollution . . . rather than the general tax paying public, but this policy does not mandate precluding a "due care" defense by imposing a

> rule that is tantamount to absolute liability for ownership of a site containing a hazardous waste.

**Id. at 361-62.**

**4. Section 107 v. Section 113**

During the early years of CERCLA, PRPs, such as a present landowner, often brought Section 107 actions against those who were culpable for the disposal of hazardous substances. These actions were based on the express language of Section 107, which clearly authorizes private parties to bring actions to recover response costs. **See 42 U.S.C. Section 9607(a)(4)(B).** In a private cost recovery action, the land owner assumed the position of the government and sought to hold arrangers, transporters, and past operators jointly and severally liable for all response costs incurred. **See Key Tronic Corp. 511 U.S. at 812 n 7.**

Judicial reception to private cost recovery actions has changed dramatically in the last five years. The question presented is whether a PRP may maintain a Section 107 "cost recovery" action, or whether the PRP must proceed with a "contribution" action under Section 113. Although there is a split of authority in the lower Courts, "every Court of Appeals that has examined this issue has come to the same conclusion: a section 107 action brought for recovery of costs may be brought only by innocent parties that have undertaken clean-ups," and a non-innocent PRP may only bring a section 113 action for contribution." **New Castle County v. Halliburton NUS Corp., 111 F.3d 1116, 1120 (3rd Cir. 1997)** (emphasis in original). The Tenth Circuit adopted this position in **United States v. Colorado Eastern R.R. Co., 50 F.3d 1530 (10th Cir. 1995)**. The First, Third, Seventh, Ninth, and the Eleventh Circuits have reached the same conclusion. **See Bedford Affiliates v. Sills, 156 F.3d 416 (2nd Cir. 1998); Pinal Creek Group v. Newmont Mining Corp., 118**

**F.3d 1298 (9th Cir. 1997); United Technologies Corp., v. Browning-Ferris Industries, Inc., 33 F.3d 96 (1st Cir. 1994), cert. denied., 513 U.S. 1183 (1995); Akzo Coatings, Inc. v. Aigner Corp., 30 F.3d 761 (7th Cir. 1994).** These Courts have found that the 1986 enactment of Section 113 indicates that Congress intended contribution to be an exclusive remedy for PRPs, that to allow PRPs to recover clean up costs under Section 107 would render Section 113 meaningless, and that the availability of Section 107 actions should be limited to governmental or "innocent PRP's for public policy reasons." **See, e.g., United Technologies, 33 F.3d at 100; Colorado Eastern R.R. Co., 50 F.3d at 1536**.

Despite the apparent trend to limit Section 107 actions by private parties, the claim has not been entirely extinguished. Section 107 historically has been used by the government to recoup the costs incurred in investigating and responding to hazardous substances. Some courts have noted that allowing "any other person" – including a PRP – to bring a 107 action is consistent with the plain language and expressed goals of CERCLA because it provides PRPs with an incentive to effectuate a prompt clean-up. **See, e.g., Companies for Fair Allocation v. Axil Corp., 853 F. Supp. 575 (D. Conn. 1994); United States v. Kramer, 757 F. Supp. 397, 416-17 (D.N.J. 1991).** Thus, several district courts have held that PRPs that are "innocent" may maintain a direct 107 action. **See Rumpke of Indiana, Inc. v. Cummins Engine Co., Inc., 107 F.3d 1235, 1239-42 (7th Cir. 1997); Boyce v. Bumb 944 F. Supp. 807, 812 (N.D. Cal. 1996);**

"Innocent" in the context of CERCLA, appears to mean "parties who [are not] themselves liable" under CERCLA, i.e., those who can establish "innocent landowner" defense under Section 101 (35) and Section 107 (b). **See, e.g., United Technologies, 33**

**F.3d at 100; Redwing Carriers v. Saraland Apts., 94 F.3d 1489, 1513 (11th Cir. 1996)** ("parties who are not themselves liable or potentially liable for response costs under Section 107 (a) of CERCLA can bring a cost recovery action directly under Section 107 (a) against potentially responsible parties"). The Fifth Circuit however, has taken a more expansive view, recognizing that "it is possible that, although falling outside of the statutory parameters" of innocence, "a PRP who spontaneously initiates a clean-up without government prodding" may maintain a direct claim under section 107 (b). **See United Technologies, 33 F.3d at 99 note 8**.

The distinction between a section 113 and section 107 is of paramount importance. In a section 107 action, the plaintiff must establish a *prima facie* case, which includes only satisfying the four elements of section 107 (a). Those elements are that: the defendant falls in one of the four categories of "responsible parties," hazardous substances were disposed of at a "facility," there was a "release" of hazardous substances into the environment, and the release caused "response costs to be incurred." **See 42 U.S.C. § 9607**. The burden then shifts to the defendant of proving that the harm at the site is divisible, and there is a reasonable basis for portioning liability for response costs. **See**, **e.g.**, **Kelley v. Thomas Solvent Co.**, **727 F. Supp. 1532, 1552 (W.D. Mich 1989)**. The practical consequence of placing this burden on defendants is that it becomes difficult to escape the joint and several liability.

In contrast, in a typical section 113 contribution action, the plaintiff must not only demonstrate that the defendant is a "covered person" under section 107, but also has the additional burden of proving each defendant's allocable share of damages. **See United States v. Taylor, 909 F. Supp. 355, 361 (M.D.N.C. 1995); United States v. Atlas Minerals**

**_____, 1995 WL 510304 at *188 (E.D. Pa. 1995)**. A PRP's "defense" to a section 113 claim also differs from a defense to a section 107 claim. Under section 107, the defendant must prove a reasonable "apportionate of harm" to establish a divisibility defense to the imposition of joint and several liability. In section 113, a defendant simply cannot be "allocated" more than its "equitable share" of several liabilities for the harm at a site. **See United States v. Western Processing Co., 734 F. Supp. 930, 938 (W.D. Wash. 1990)**. Thus, even if a defendant cannot show a reasonable basis for apportioning the harm (which is a defense to a section 107 claim) a defendant in a section 113 contribution proceeding can rely on any number of "equitable factors" to allocate that defendant's proportionate share of response costs.

**5. Limiting Liability for Passive Migration**

In the CERCLA early years, a landowner could be liable as a "covered person" under section 107 if contaminants migrated through the groundwater and underneath her property. The majority of courts that addressed this issue viewed passive migration of contaminants as a form of "disposal" under CERCLA. **See, e.g., Nurad, 966 F.2d at 845; Stanley Works, 781 F. Supp. At 664.** In the latter half of the 1990s, courts have retracted the meaning of "disposal" and have held that passive migration of contamination does not implicate CERCLA liability unless a party acted in a manner which promoted the migration through the soil or groundwater. **See, e.g., ABB Industrial, 120 F.3d at 358-59; CDMG Realty, 96 F.3d at 713; 150 Acres of Land, 204 F.3d at 698.**

**6. Restricting Lender Liability**

Section 101 (20) of CERCLA includes a security interest holder exemption that

excludes from liability those who, without participating in the management of a facility, hold "indicia of ownership" primarily to protect a security interest. **42 U.S.C. § 9601(20)**. The Eleventh Circuit in **United States v. Fleet Factors Corp., 901 F.2d 1550 (11th Cir. 1990), cert. denied, 498 U.S. 1046 (1991)**, caused considerable concern within the lending community by holding that a lender who has the ability to participate in the management of a business cannot avail itself of the exemption. Additionally, the exemption disappeared once the lender obtained title through foreclosure, since the lender now held title rather than an "indicia of ownership."

In response to the **Fleet Factors** decision, EPA issued a rule clarifying the scope of the security interest exemption to provide lenders with certain a safe harbor. **See 57 Fed. Reg. 18,344 (April 29, 1992)**. This rule was immediately challenged in **Kelley v. EPA, 15 F. 3d 1100**, **reh'g denied**, **25 F.3d 1088 (D.C. Cir. 1994), cert. denied, American Bankers Association v. Kelley, 513 U.S. 1110 (1995)**. The D.C. Circuit vacated EPA's rule, holding that an administrative agency has no authority to issue regulations defining the liability under Section 107 of CERCLA. The Court declared that, when lenders are named as defendants under CERCLA, the "claim . . . should be evaluated by the federal courts independent of EPAs institutional views." **Id. at 1109.**

Congress responded to the invalidation of EPA's "safe harbor" rule by passing the Asset Conservation, Lender Liability and Deposit Insurance Protection Act of 1996 "ACA," 110 Stat. 3009–462. The law amended the secured creditor exemption of CERCLA and essentially validated EPA's lender liability rule. The ACA states that secured lenders who do not participate in management are not owners or operators within the meaning of

CERCLA and therefore not liable for response costs. Additionally, the ACA provides that lenders may take certain actions prior to and after foreclosure without invalidating the secured creditor exemption. A lender may:

1. Sell, lease or liquidate the facility in question;
2. Maintain business activities or wind-up operations at a facility; or
3. Undertake response actions with respect to hazardous substance contamination.

The aforementioned activities are exempted only if the lender is actively attempting to divest itself of the facility "at the earliest practicable, commercially reasonable time, on commercially reasonable terms, taking into account market conditions and legal and regulatory requirements." **42 U.S.C. § 9601(20)(E)(ii).**

The ACA also clarified the types of activities in which lenders may engage and not specifically "participate in management." These include:

1. Providing financial or administrative advice and assistance to the borrower;
2. Restructuring a loan agreement;
3. Possess the capacity to influence facility management, or the unexercised right to control operations;
4. Ensuring compliance with environmental terms of the loan agreement; and
5. Requiring environmental response actions to be undertaken by the borrower, or directly undertaking such actions itself.

## VI. REUSE OF ENVIRONMENTALLY IMPAIRED PROPERTY

### A. Brownfields

The EPA defines "Brownfields" as "abandoned, idled, under-used industrial and commercial facilities where expansion or redevelopment is complicated by real or perceived environmental contamination." **See Brownfields Economic Redevelopment Initiative (September of 1995)**. While many factors have caused investors to shy away from Brownfields properties, CERCLA created the essential risk associated with ownership of previously contaminated sites. As discussed in Part V above, CERCLA's liability scheme imposed liability for the costs of clean-ups on a number of classes of "responsible parties," including current owners and operators of a contaminated site who arguably had nothing to do with the contamination. Against this backdrop, the unattractiveness of an old industrial or commercial site is readily understandable.

The EPA has expressly acknowledged that CERCLA has acted as a significant impediment to the development of Brownfield properties, which are often located in low income or other depressed areas. In order to address this problem, Congress has afforded protection to lenders under the Asset Conservation, Liability and Deposit Insurance Protection Act, also discussed in Part V above. However, the main focus of the EPA and of the States has been to encourage development without the risk of incurring unnecessary liability. The EPA has two primary mechanisms for the clarification and liquidation of potential liability, both of which are discussed below:

### 1. Comfort letters

The purpose of comfort letters is to provide prospective purchasers and others with the best, current information about the EPA's interest, or lack thereof, in a given site. These letters summarize data available to the EPA regarding a site and, importantly, summarize the federal government's past actions and future expectations with respect to response actions at the site. The EPA will not issue a comfort letter for any property unless there is a realistic perception or a probability of a prospective new owner incurring CERCLA liability. The EPA policy, which may be found on the EPA website, sets out four types of sample comfort/status letters:

a. A "no previous federal Superfund interest" letter advises party that there is no evidence of past Superfund interest or involvement with the site (in other words, the site is not in the CERCLIS database).

b. A "no current federal Superfund interest" may advise a prospective purchaser that this site has been deleted from CERCLIS or from the National Priorities List.

c. A "federal interest" letter advises the prospective purchaser that the EPA is responding, or plans to respond, to contamination at a site.

d. A "State Action" letter indicates that the State has primary responsibility for any activities at this site.

### 2. Prospective Purchaser Agreements ("PPAs")

In contrast to a comfort letter, a PPA provides actual resolution or liquidation of any legal liability that the prospective purchaser might incur. EPA issued its guidance on agreements with prospective purchasers of contaminated property on May 24, 1995, which states that PPAs are available only for sites where there has been, or where there realistically will be, a CERCLA response action. This standard is more restrictive than that which governs the issuance of comfort letters. The essence of a PPA is a covenant not to sue the new owner for pre-existing contamination, which is generally granted in exchange for appropriate consideration. The covenant not to sue also qualifies pursuant to section 113 (f) (2) of CERCLA, to protect the new owner from possible contribution actions by other PRPs.

The EPA guidance states that in consideration of granting the covenant not to sue, the EPA should receive a substantial benefit either in the form of a clean-up, or an indirect public benefit in combination with a reduced direct benefit to EPA. Prior versions of the guidance restricted the consideration to direct benefits of cash or clean-up work. However, the current guidance recognizes the considerable indirect benefit that can be realized from Brownfields redevelopment, including the creation or retention of jobs, the development of abandoned or blighted property, the creation of conservation or recreation areas, or the improvement of public transportation or infrastructure.

## I. OVERVIEW OF ENVIROMENTAL REGULATION

The regulatory climate for development has changed markedly in the past decade. In

addition to zoning and subdivision issues, the astute developer must analyze a multitude of environmental issues prior to reducing the project to a blueprint. As recently as five years ago, most development projects were shelved permanently if an initial investigation revealed existing environmental problems which potentially implicated liabilities under the far-reaching federal and state regulatory schemes. Financing for these projects could not be obtained, and no one, including the developer itself, was desirous of inheriting a project laden with potential environmental liabilities.

Times have changed at a pace that is remarkable in the regulatory field. The United States Environmental Protection Agency ("EPA") has itself recognized the impediment to development that the Superfund, or Comprehensive Environmental Response, Compensation, and Liability Act of 1980 ("CERCLA"), has imposed on innocent parties. Congress has finally vested lenders with a true "safe harbor," and the advent of brownfields legislation and guidance documents have encouraged, rather than frustrated, the development of environmentally blighted properties. In fact, the regulatory agencies have shifted their focus from an "all-out" remedial effort to a "risk based" response designed to assist developers in placing the property to its highest and best use.

This paper will review a common sense approach to developing an environmental baseline, which segregates existing environmental conditions from those which may develop after the closing of the purchase of the property. After discussion of the environmental baseline, this paper will address the primary environmental permits necessary for a successful development, including air quality, hazardous waste, and wetlands issues. This presentation will then highlight the historical theories of liability and the limited defenses to

environmental claims asserted under federal law, and compare that history to the recent judicial trend of expanding those defenses and thereby encouraging property development. Finally, the ability to "reuse" environmentally impaired properties will be discussed. The development of these impaired properties, commonly known as "brownfields," will be affected by the structure of the environmental baseline, the relief afforded to lenders providing the financing for the project, and by the recent judicial limitations on liability and the expansion of defenses available under federal law.

## II. ENVIRONMENTAL BASE LINE

In virtually every business development transaction, potential environmental liability is a risk that must be appropriately assessed. As the discussion of the Comprehensive Environmental Response, Compensation and Liability Act, 42 U.S.C. 9601 et. seq. ("CERCLA") in part V below indicates, liability is frequently based not as much on fault as on ability to pay. Additionally, future laws may impose potential construction or operational restrictions which may deprive a proposed project of economic viability. The role of the environmental attorney is to ensure that these risks are managed to achieve maximum value.

Environmental risks in buying or selling real estate can be segregated into the following four categories: (i) existing contamination of purchased property, which is largely governed by CERCLA; (ii) third-party claims which may be asserted by neighboring land owners; (iii) operational restrictions, including obtaining necessary environmental permits and compliance with those permits; and (iv) enforcement actions, which may be instituted by an agency or an aggrieved citizen based on activities which preceded the purchase.

### B. Due Diligence

A properly conducted environmental review of a property or business should be designed to quantify known and perceived risks. Appropriate due diligence includes an identification of environmental conditions, a determination of whether those conditions must be remedied, the cost of any remedy, and the likelihood of third-party claims. These questions are initially answered by a Phase I Environmental Assessment, performed in accordance with the American Society for Testing of Materials ("ASTM") Phase I Standards. If a "Recognized Environmental Condition" potentially exists at the site, a Phase II Environmental Site Assessment may be warranted.

**1. Sources of Due Diligence Information**

a. Site History

1. Review of background information
2. In-house facility records review
6. Environmental records
7. Regulatory files
8. History of discharges
6. History of environmental citations
7. History of chemical material storage

b. Review of past operations on site

c. Review of state environmental records

d. Review of EPA records

e. Review of health records

f. Title search

g. Review of local tax assessor files

h. Site walk-through

1. Pre-walk through meeting with contact person to discuss current operations and past operations

4. Review on-site process operations

5. Review on-site materials

i. Review and observe environmental setting

j. Zoning

k. Proximity to residential areas

1. Proximity to water bodies

2. Proximity to wetlands

l. Physical inspection of all buildings and grounds (exterior and interior)

m. Review blueprints of the facility

n. Review storm sewers

o. Review leach fields

p. Review dry wells

q. Review process lines

r. Review sumps

s. Review floor drains

t. Review building vents

u. Review transformers

v. Physically trace handling of all hazardous materials and wastes to confirm any descriptions provided in records and operation manuals or narratives

w. Review possible migration pathways

x. Review all environmental permits

2. Determine nature and scope of permits

y. Review all site maps

z. Review all heating systems

aa. Review wastewater discharges

bb. Review hazardous substances

3. conduct waste inventory

4. check against company records

cc. Review all Material Safety Data Sheets ("MSDS")

dd. Review all OSHA requirements

ee. Review all hazardous substance containment facilities

7. note materials stored

8. note construction of storage containers

9. note storage units and include size, location and age

10. conduct necessary interviews with all operators and employees

11. conduct interviews with former employees and operators

12. consider Freedom of Information Act request to determine if there have been any alleged violations of any federal laws relating to hazardous materials or whether any enforcement actions have been brought against this owner or prior owners.

ff. Review all aerial photographs (if not immediately available, consult commercial sources)

1. Aerial photographs of most areas of the country are available for purchase commercially

2. Site photos are generally taken at ten-year intervals or less.

gg. Review all surrounding and neighboring uses

hh. Conduct appropriate physical and chemical screening tests

5. Direct read instrumentation (equipment that analyzes gas or vapor directly with the instrument displaying a measured value on a gauge)

6. Portable gas chromatograph: direction of soil vapors through chromatograph shows parameters to be separated and upon separation the target materials are measured using a sensor.

7. Metal detectors: confirm presence of underground tanks.

8. Field Test Kit: Detection of polychlorinated biphenyls ("PCB")

ii. Conduct, where appropriate, laboratory analysis of field samples

jj Analyze soils, sediments and sludges

e. Sample at or around underground tanks

f. Sample at or around piping areas

g. Physically collect samples

h. Laboratory analysis of collected samples

kk. Groundwater Analysis

d. Well installation

e. Sample collection

f. Laboratory analysis

**2. Representations and Warranties**

Common subjects for representations in connection with environmental matters include the following:

e. Compliance with laws and regulations;

f. Possession and effectiveness of required permits;

g. Lack of pending or threatened enforcement action; and

h. Lack of pending or threatened third-party claims.

Additionally, a buyer should require representations of the seller concerning the absence of undisclosed liabilities and whether hazardous substances have been used or stored on the property.

From the seller's perspective, an "AS IS" clause may not be sufficient to prevent the buyer from seeking reimbursement for environmental costs, as these types of clauses are generally construed against the seller. **Southland Corp. v. Ashland Oil Inc., 696 F. Supp. 994 (D.N.J. 1988)**.

**3. "As Is"**

Buyer agrees that, except as expressly set forth in this agreement, no representations by or on behalf of Seller have been made to Buyer as to the condition of the property, any restrictions related to the development of the property, the applicability of any governmental requirements, including, but not limited to "environmental requirements" pertaining to the property, or the suitability of the property for any purpose whatsoever. Buyer represents to Seller that Buyer has made its own independent investigation of the property and is relying solely on such independent investigation. Buyer acknowledges that Seller has no expertise concerning "environmental requirements" and "hazardous materials" and that Buyer is not relying on any representation or the lack of same, with respect to "environmental requirements" or "hazardous materials" as they apply to conditions on the property.

Through the environmental due diligence procedure, the parties are able to segregate pre-closing from post-closing liabilities. This segregation, commonly called the "Environmental Baseline," serves to establish responsibilities for environmental response costs and liabilities which are liquidated after the closing of the purchase and sale.

The following are examples of allocation and baseline provisions:

**4. Environmental Allocation**

Except as otherwise provided in this schedule, Seller shall be responsible for, and bear the costs of, such corrective action as may arise as a consequence of the ownership or operation of the property prior to the closing date, and Buyer shall be responsible for, and bear the cost of, such corrective action as may arise as a consequence of the ownership or operation of the property on or after the closing date. The presence or absence or hazardous

substances in the soil or groundwater on the property as of the closing date, for purposes of determining the necessity of corrective action, shall be conclusively determined by the baseline, as defined below.

**5. Environmental Baseline**

Except as otherwise provided, or specifically agreed to in writing, the presence or absence as of the closing date of hazardous substances in the soil or groundwater on the property, or that have migrated or may migrate from the property as a consequence of activities on or related to the property (hereinafter called the "Environmental Baseline"), shall be determined referenced to data from the environmental assessments performed by ABC Company. The Environmental Baseline shall not include the presence of substance in such quantities as are consistent with the method of operation of the property, in process equipment, storage tanks, land farm, or non-earth containment devices or of such substances as may lawfully exist as a consequence of the operation of the property ("lawful substances"). Buyer agrees to be responsible for any corrective action arising from the use of lawful substances after the closing date, and any contamination caused by those lawful substances after the closing date or related corrective action after the closing date.

## III. PRIMARY ENVIRONMENTAL PERMITS

### D. Air

#### 1. Construction Permit

Under the New Mexico Air Quality Control Act, **N.M. Stat. Ann. §§74-2-1 et. seq. (1978)**, the Environmental Improvement Board is designated as the state air pollution control

agency. **N.M. Stat. Ann. § 74-2-3(B)** Section 74-2-7 requires an air quality permit for the construction or modification for the construction or "modification" of any new source. "Air pollution" is defined as

> "[t]he emission, except emission as occurs in nature, into the outdoor atmosphere of one or more air contaminants in such quantities and duration that may with reasonable probability injure human health, animal, or plant life or as may unreasonably interfere with the public welfare, visibility, or the reasonable use of property."

**N.M. Stat. Ann. § 74-2-2(B)(1978).**

### 3. Regulation 702

Although often misunderstood by industry, Regulation 702 is not properly viewed as an operational permit. It addresses construction permits which are required before operation of an air pollutant "source" can occur. Consequently, environmental modeling studies must be completed well before construction, and must identify levels of potential emissions. Those emissions typically include Nitrous Oxide, Carbon Monoxide, and Non-Methane Hydrocarbons.

Part II of Regulation 702 provides that permits "must be obtained" from the Environment Department under the following circumstances: (i) prior to the construction of a source which emits one or more regulated air contaminants for which there is a national ambient air quality standard or state ambient standard and which emits greater than ten pounds per hour of any regulated air contaminant or has a potential emission rate of greater than one hundred pounds per hour; and (ii) toxic air pollutants. Oil and gas operations, including distribution facilities, are exempt from the toxic air pollutant requirements. Consequently, the pertinent regulation is that which restricts emissions of certain designated

constituents to ten pounds per hour.

Typically, the Environment Department will notify the applicant concerning the completeness of the permit application within thirty days after the application has been submitted. After notification of the completeness or lack thereof, the Environment Department is allowed one hundred twenty days to conclude the processing of the permitting application. Accordingly, an applicant may reasonably expect a one hundred-fifty day waiting period prior to the issuance of an air quality permit.

Many operators have concluded that a permit is not necessary if a catalytic converter or other device will reduce anticipated emissions below regulatory standards. The applicability of the permitting requirements is generally based on levels of uncontrolled "potential" emissions.

**E. Water**

The Federal Clean Water Act prohibits the discharge of pollutants by any person into navigable waters except in compliance with specified requirements of the Act. **33 U.S.C. §§1251 et. seq.**

3. Point Source Discharges

"Point Source" is defined in the Clean Water Act as "any discernable, confined and discrete conveyance, including but not limited to any pipe, ditch, channel, tunnel . . ." **33 U.S.C. § 1362(14)**. Point source discharges are prohibited unless authorized by a National Pollutant Discharge Elimination System Permit ("NPDES"). Traditionally, point source discharges have been deemed to be "discrete" discharges, from a source that is readily discernable. **See Hudson Riverkeeper Fund, Inc. v. Harbor at Hastings**

**_____, 917 F. Supp. 251, 257 (S.D.N.Y. 1996)**. However, the United States District Court for the District of Oregon recently held that cattle grazing constitutes a point source because the activity "may" result in water pollution. **See Oregon Natural Desert Ass'n v. Thomas**, **940 F.Supp 1534, 1541 (D.Or. 1996), overruled by Oregon Natural Desert Ass'n v. Bombeck, 172 F.3d 1092 (9th Cir. 1998)**. The difference between a "point source" and non-point source discharge is significant. All point source discharges are subject to the NPDES permitting program, whereas non-point source discharges generally are not so regulated.

The NPDES permitting program is the primary method by which pollutants can be added to waters of the United States in compliance with the Clean Water Act's discharge prohibition. NPDS permitting is accomplished pursuant to section 402 of the Act. **C.**

**Storm Water Permits**

The Clean Water Act has evolved to the point where NPDS permit requirements are imposed on storm water discharges. However, since the early 1990s, the EPA has established ten nation-wide permits available for developers. These nation-wide permits require the filing of a Notice of Intent prior to construction and additional requirements concerning the observation and reporting of any pollutants which accumulate in storm water run-off.

**D. Wetlands Permit Section 404**

See Wetlands discussion in part IV below.

**F. Hazardous Waste Permitting**

**1. 42 U.S.C. § 6928(d)(1)**

Prohibited Act: Transport hazardous waste to a facility which does not have a permit.

**2. 42 U.S.C. § 6928(d)(2)**

Prohibited Act: Treat, store or dispose of any hazardous waste, without a permit, or in violation of a material condition of a permit, or in violation of any material condition of any interim status regulations or standards.

**3. 42 U.S.C. § 6928(d)(3)**

Prohibited Act: Omit material information or make any false material statement or representation for purposes of compliance with state or federal RCRA regulations.

**4. U.S.C. § 6928(d)(4)**

Prohibited Act: Generate, store, treat, transport, or dispose of, or otherwise handle any hazardous waste or destroy, conceal, or fail to file any required record.

**5. 42 U.S.C. § 6928(d)(5)**

Prohibited Act: Transport any hazardous waste without a required manifest.

**6. 42 U.S.C. § 6928(d)(6)**

Prohibited Act**:** Export a hazardous waste without the consent of the receiving country, or in a manner inconsistent with an international agreement.

## IV. WETLANDS REGULATION

The primary statutory provision regulating development in Wetlands is section 404 of the Clean Water Act ("CWA"), **33 U.S.C §1344**. The Clean Water Act prohibits the discharge of pollutants from discrete point sources into waters of the United States. **Id. § 1311(a)**. However, Congress authorized the Army Corp of Engineers under section 404 of the CWA to administer a separate permit program for discharges of dredged or fill material. This section has evolved into the federal government's primary tool to limit development in Wetlands.

Discharges of dredged and fill material have been defined so broadly that many development activities in jurisdictional Wetlands will involve a regulated discharge. The courts generally define "discharge of dredge material" as the addition of material excavated or dredged from waters of the United States, including run-off from a dredge material disposal area. **33 C.F.R. § 323.2(d)(1)**. In response to the settlement of civil citizens' suits which were critical of the Corp's regulations, the Corp adopted a strict view of regulating dredging operations.

Similarly, "discharge of fill material" is a broad category, covering almost every activity that involves earth moving or discharges into designated Wetlands. Among the regulated activities are "placement of fill that is necessary for the construction in a water of the United States; the building of any structure or impoundment requiring rock, sand, dirt or other material for a construction; site – development fills;" causeway or road fills; and many other protection devices. **33 C.F.R. § 323.2(f)(1997)**. Even the temporary stockpiling of soil from the construction of a drainage ditch or similar excavation may be a regulated

discharge. **A. Section 404 Permit Process**

In view of the expansive definition of dredging and discharging operations, all Phase I assessments should include a determination of whether the proposed development is in an area designated by the Corp as a Wetland. Maps maintained by the Corp and by the Fish and Wildlife Service may be found on EPA's Wetlands website: http:\\www.epa.gov\owow\wetlands\. Under the 1989 Interagency Federal Manual for Identifying and Delineating Jurisdictional Wetlands, three criteria must be present for an area to be considered a Jurisdiction Wetland: Wetland vegetation, hydric soils, and Wetland hydrology. The manual also provides that, in certain circumstances, the presence of one of the criteria may be presumed from the presence of the other two. If the proposed development is in a designated Wetland area, a section 404 permit must be obtained from the Corp of Engineers.

There are two types of section 404 permits - individual and general. The Corp issues general permits for categories of activities that involve only minimal environmental disruption. General permits may be issued on either a nation-wide or on a regional basis. Consequently, it is necessary to investigate the applicable general permits and, if appropriate to redesign the project so it falls within the parameters of a general permit.

**W. CERCLA**

**A. Background**

Congress enacted the Comprehensive Environmental Response, Compensation and Liability Act ("CERCLA") in 1980, in an effort to control further damage to sites contaminated by hazardous substances. Ever since that time, the term "environmental

liability" has taken on new meaning for American businesses. CERCLA is unusual - it imposes harsh concepts of liability on responsible and innocent parties alike, notwithstanding the fact that the environmental problems addressed by CERCLA have usually developed over long periods of time with involvement by numerous companies and individuals.

This part of the presentation addresses the historical concepts of liability under CERCLA, including liability traditionally imposed upon present owners of land, prior owners, successor owners of corporations, and lessees. After a discussion of the historical theories of liability, this paper addresses the recent expansion of the previously limited defenses available to potentially responsible parties. Finally, this presentation addresses contribution rights among parties who are potentially liable under CERCLA, and Congress's recent efforts to limit the scope of CERCLA liability for lenders.

### B. Historical Theories of Liability

#### 1. CERCLA Imposes Broad Liability

In the event that hazardous substances have been "released" from "a facility," **see 42 U.S.C. § 9601(22)**, four groups of defendants may be liable for environmental response costs incurred by the government or by a private party plaintiff. The breadth of liability has not been limited to those who are culpable, in one way or another, for the environmental degradation. The group of defendants includes: (i) the current owner, whose only mistake may have been to purchase the property, and the current operator; (ii) past owners and operators at any time during which the disposal of hazardous substances occurred; (iii) persons who arranged for disposal of those substances; and (iv) the transporters who selected

the ultimate disposal site. **See 42 U.S.C. § 9607(a)**. There is no necessity under CERCLA for a private party plaintiff or the government to show that any of the four potential groups of defendants was negligent or wrongfully conducted activities at the site. On the contrary, CERCLA imposes strict liability, **United States v. Davis, 261 F.3d 7, 28 (1st Cir. 2001)** and the lawfulness of the previous activities at the site is irrelevant to the imposition of that liability, **see State of New York v. Shore Realty Corp., 759 F.2d 1032, 1043-1044 (2nd Cir. 1985).**

In addition to the abandonment of culpability under CERCLA, any and all of the four potential groups of defendants have traditionally been jointly and strictly liable for indivisible pollution. **See, e.g., Sun Co., Inc. v. Browning-Ferris, Inc., 124 F.3d 1187, 1189 (10th Cir. 1997);United States v. Chem-Dyne, 572 F. Supp. 802, 805-10 (S.D. Ohio 1983).** Accordingly, it has been the defendant's burden to prove that her individual contamination may be sufficiently segregated and apportioned for purposes of liability. Given the complexities of groundwater management and the somewhat theoretical nature of hydrology, one can easily conclude that this burden is extremely difficult, if not impossible, to establish at trial. This problem is exacerbated by the fact that the plaintiff need not prove that there is a causal link between the hazardous substances deposited by the defendant and the hazardous substances which have actually caused damage to the environment. **See, e.g., Chem-Dyne, 572 F. Supp. 802 (S.D. Ohio 1983). But see recent developments discussed in paragraph V H3 below.**

In the early 1990s, the Second and Third Circuits addressed the question of divisibility of harm. In separate cases involving the same parties, both Courts adopted the

position that a defendant may escape liability if it can show that "its pollutants, when mixed with other hazardous wastes, did not contribute to the release or the resulting response costs." **United States v. Alcan Aluminum Corp., 990 F.2d 711, 717 (2nd Cir. 1993); see United States v. Alcan Aluminum Corp., 964 F.2d 252 (3rd Cir. 1992).** This determination will depend on the facts of each case, but it remains the defendant's burden to show divisibility. **U.S. v. Alcan, 964 F.2d at 269.**

Yet another approach to the division of joint and several liability was adopted in **United States v. A & F Materials Co., Inc., 578 F. Supp 1249 (S.D. Ill. 1984)**. There the Court looked to whether there is a reasonable basis on which to apportion liability. If it finds none, the Court may nonetheless decline to impose joint and several liability if the result would be inequitable. **See In the Matter of Bell Petroleum Services, Inc., 3 F.3d 889 (5th Cir. 1993)** (discussion of the evolving approaches to joint and several liability). Whether the harm suffered by the plaintiff is apportionable is a question of law. **Id. at 902.**

### F. Theories of Liability Against Present and Prior Owners

#### 1. Present Owner Liability.

42 U.S.C. § 9607(a) provides that persons liable under CERCLA include: "(1) The owner . . . of . . . a facility . . . ." Thus, probably the most appropriate way to define the theory of liability against a present owner of property is that of a "status tort." **See Moskowitz, Environmental Liability and Real Property Transactions, 48 (1989).**

The imposition of absolute liability on present, innocent owners is somewhat ironic, particularly considering the expressed intent of Congress in enacting CERCLA. CERCLA was enacted because "Congress intended that those responsible for problems caused by the

disposal of chemical poisons bear the costs and responsibility for remedying the harmful conditions they created." **United States v. Reilly Tar & Chem. Corp., 546 F. Supp. 1100, 1112 (D. Minn. 1982).** According to one author and a variety of courts, the theme of CERCLA was "the imposition of liability for the effects of past disposal practices . . . on those who created and profited from waste disposal - generators, transporters, and disposal site owner/operators." **See Moskowitz, supra at 49; United States v. Northeastern Pharmaceutical & Chemical Company, 579 F. Supp. 823, 840 (W.D. Mo. 1984)** ("Congress intended to have the chemical industry, past and present, pay for the costs of cleaning up inactive hazardous waste sites."). **See, also, United States v. Bliss, 667 F. Supp. 1298, 1304 (E.D. Mo. 1987); overruled on other grounds by U.S. v. Davis, 794 F.Supp. 67 (D.R.I. 1992); United States v. Price, 577 F. Supp. 1103, 1114 (D.N.J. 1983).**

Where does this leave the person who is not a chemical manufacturer and who purchased the site without knowing that it had previously been used for disposal activities? The so-called "polluter pays" policy simply has no application in this situation. Thus, it has been suggested that in 1980, Congress mistakenly attached absolute liability to innocent owners by a drafting error. By 1986, however, due to the increased costs associated with remediation, no one had seriously questioned the liability of the innocent, present owner. **See Moskowitz, supra, at 49.** This liability was solidified by the Superfund Amendments and Reauthorization Act of 1986, Pub. L. No. 99-499, 100 Stat. 1613 (1986) ("SARA"), which states that the liability of present owners includes those who acquired "title or possession" through "land contracts, deeds or other instruments." **42 U.S.C. § 9601(35)**.

The theories of liability against present owners have mushroomed. The definition of

"owner" has been extended by one Court to include a lessee or a sublessor. **See United States v. South Carolina Recycling & Disposal, Inc., 653 F. Supp. 984 (D.S.C. 1984).** Another Court conferred ownership status on a beneficiary of a trust who, by definition, did not possess any indicia of legal ownership. **See United States v. Burns, 1988 WL 242553 (D.N.H. 1988).**

**2. Prior Owner Liability.**

Prior owners of a site are liable under 42 U.S.C.A. § 9607(a)(2), which states as follows:

> [A]ny person who at the time of disposal of any hazardous substance owned . . . any facility at which such hazardous wastes were disposed of . . .

**42 U.S.C. § 9607(a)(2).**

While some authors have suggested that current theory imposes liability on anyone in the "chain of title" of a particular property, the precise language of Section 9607 (a)(2) is to the contrary. **See Moskowitz, supra, at 50.** The literal interpretation of the section appears to require a finding of ownership during the time of disposal before liability can attach. Consequently, before the enactment of SARA in 1986, it was possible for an owner of a property to avoid liability simply by transferring title. SARA expressly closed this loophole by providing the following in 42 U.S.C. § 9601 (35)(C):

> [I]f the defendant obtained actual knowledge of the release or threatened release of a hazardous substance at such facility

> when the defendant owned the real property and then subsequently transferred ownership of the property to another person without disclosing such knowledge, such defendant shall be treated as liable . . . and no defense . . . shall be available to such defendant.

**42 U.S.C. § 9601(35)(c)** (emphasis added).

It therefore appears that the following types of prior owners may avoid liability: (i) those without knowledge of the contamination; and (ii) prior owners with knowledge who conveyed the property with adequate disclosures. However, a significant barrier exists in order to employ the escape route provided by 42 U.S.C. § 9601(35)(C). If there has been a "disposal" during your client's period of prior ownership, the exception of 42 U.S.C. § 9607(a)(2) is unavailable. **See United States v. Price, 523 F. Supp. 1055 (D.N.J. 1981), aff'd, 688 F.2d 204 (3d Cir. 1982)** ("disposal" includes continued leaking during the period of ownership); **Tanglewood East Homeowners v. Charles-Thomas, Inc., 849 F.2d 1568 (5th Cir. 1988)** (grating of property constitutes disposal).

With respect to prior owners, one author has suggested that the best reading of CERCLA is that a prior owner has no liability and therefore no need for a defense if (i) she purchased the property after the release was completed and (ii) she either (a) sold the property with ignorance of the release or (b) disclosed the release to the purchaser. **42 U.S.C. § 9607(a)(2)**. **See Moskowitz, supra, at 53.**

### D. Traditional Defenses Available Under CERCLA

#### 1. Third-Party Defense – Present Owners.

An innocent purchaser may avoid liability if he can establish that the release or threat of release was caused solely by:

> An act or omission of a third party other than an employee or agent of the defendant, or than one whose act or omission occurs in connection with a contractual relationship, existing directly or indirectly, with the defendant . . .

**See 42 U.S.C. § 9607(b)(3)** (emphasis added). Innocent owners have been plagued by the inarticulate drafting of the "third-party" defense. The "third-party" defense is not available if (i) the release occurred "in connection with a contractual relationship, existing directly or indirectly, with the defendant," or (ii) if no contractual relationship existed and the release was not solely caused by another. **Id**. It is difficult to determine precisely what this means. Under SARA, the term "contractual relationship," for the purpose of § 9607(b)(3), includes "land contracts, deeds or other instruments transferring title or possession . . ." **See 42 U.S.C. § 9601(35)(A); see also, United States v. Monsanto Co., 858 F.2d 160, 169 (4th Cir. 1988).** Arguably, every present owner has a contractual relationship, in some way or another, with a previous polluter in her chain of title.

It is absurd to suggest that a deed or lease or any other "contractual relationship" transferring possession explains how any pollution caused by a predecessor was done "in connection with" a contractual relationship. Nonetheless, Courts have used the mere existence of a contractual relationship, wholly divorced from any connection with the activities of the polluter, to impose liability on a subsequent owner. **See, e.g., United States of America v. Monsanto Co., 855 F.2d 160, 169 (4th Cir. 1988).**

**2. SARA "Due Diligence" Defense.**

Because of the implausibility of the third-party defense and the broad nature of "a contractual relationship" with a previous polluter, SARA has provided some minimal

relief in the form of the due diligence defense. Thus, there is an exception to liability through the "contractual relationship" where:

> [T]he real property on which the facility concerned is located was acquired by the defendant after the disposal or placement of the hazardous substance on, in, or at the facility, and . . .
>
> (i) At the time the defendant acquired the facility the defendant did not know and had no reason to know that any hazardous substance which is the subject of the release or threatened release was disposed of, on, in or at the facility.

**42 U.S.C. § 9601(35)(A)**. This language therefore requires complete innocence on the part of the new owner. A new owner must not have caused the pollution, he must not have been there when it was caused, and he must not know about it when the property was acquired. Plainly, the drafters of CERCLA attempted to promote so-called "due diligence" investigations prior to the acquisition of property. **See United States v. Pacific Hidet Fur Depot Inc., 716 F. Supp. 1341 (D. Idaho 1989)** (defense available); **O'Neil v. Picillo, 682 F.Supp. 706 (D.R.I. 1988) aff'd., 883 F.2d 176 (1st Cir. 1989)** (defense not available - release not caused "solely" by a third party); **United States v. Hooker Chem. & Plastics Corp., 680 F. Supp. 546 (W.D.N.Y. 1988)** (third party defense not available); **United States v. Serafini, 706 F. Supp. 346 (M.D.Pa. 1988)** (question of fact precluding summary judgment as to customary practice in acquiring contaminated site in 1969); **State of Washington v. Time Oil Co., 687 F. Supp. 529 (W.D. Wash. 1988)** (innocent landowner defense rejected where company failed to show that it exercised due care with respect to hazardous substances on property); **United States v. Mottolo, 695 F. Supp. 615 (D.N.H. 1988)** (due diligence defense not available where third parties were not the sole cause of

contamination).

### 3. No Recovery of Costs for Actions Inconsistent with the National Contingency Plan.

Defendants may also escape liability for recovery of any cost incurred by the government which is inconsistent with the National Contingency Plan. The burden is on the defendant to show the government's chosen response action was inconsistent with the Plan and that the government acted arbitrarily and capriciously in choosing that response action. **U.S. v. Hardage Steering Committee, 982 F.2d 1436, 1442 (10th Cir. 1992) cert. denied, 510 U.S. 913 (1993); see also U.S. v. Northeastern Pharmaceutical & Chemical Co., Inc., 810 F.2d 726 (8th Cir. 1986) cert. denied, 484 U.S. 848 (1987).** An excessive cost can be challenged if the defendant argues that the government arbitrarily and capriciously failed to consider cost as a factor when deciding on the appropriate response, or selected a response action that was not cost-effective. **Hardage, 982 F.2d at 1443**.

### 4. Contribution no more than Background Contamination.

The Second Circuit, in **United States v. Alcan Aluminum Corp., 990 F.2d 711 (2nd Cir. 1993)**, denied the government's motion for summary judgment and allowed Alcan to argue that it should have no liability for clean-up costs if it could show that its oil emulsion, when mixed with other wastes, did not contribute to the releases at the site or to the clean-up costs. Alcan suggested that its oil emulsion waste contributed no hazardous substances to the site. While allowing the argument, the Court put the burden of proof on the defendant. The decision in **Alcan Aluminum Corp.** was one of the first to recognize a limited exception to the no causation or strict liability rule where EPA thresholds for a

pollutant are absent.

**E. Summary Liabilities and Defenses**

**1. Prior Owners.**

A prior owner should not need a defense under CERCLA if the statute imposes no liability. Thus, if the prior owner had not performed adequate due diligence, the only consequence should be the unavailability of the "innocent purchaser" defense. **See Moskowitz, supra, at 53**. But if the prior owner did not own the property during the time of disposal, no liability should attach under the express language of 42 U.S.C. § 9607 (a) (2). Thus, it appears that CERCLA and the SARA amendments should not impose liability upon prior owners if the prior owner purchased the property after the release and subsequently sold the property (i) without knowledge of any release or (ii) after disclosing the release to the purchaser.

**2. Present Owners**

With respect to present owners, CERCLA provides little, if any, relief. To avoid liability, present owners must establish that the pollution was caused solely by the actions of other parties and that the release either (i) did not occur in connection with a contractual relationship (the third-party defense, which has traditionally been meaningless); or (ii) the release occurred in connection with a contractual relationship, but the elements of the due diligence defense have been satisfied.

**3. Successor Liability.**

The general rule is that merging a liable corporation with another corporation is an ineffective means to avoid the transfer of liability. In such a situation, the liability

simply follows the corporation, regardless of the identity of the new owner or its shares. **Id. at 91**. On the other hand, it may be possible to acquire the assets of a corporation without acquiring unrelated liabilities. **See Smith Land & Improvement Corp. v. Celotex Corp., 851 F.2d 86, 91 (3rd Cir. 1988) cert. Denied, 488 U.S. 1029 (1989). But see Ortiz v. South Bend Lathe, 46 Cal. App. 3d 842, 846, 120 Cal. Rptr. 556 (1975)** (transfer of contaminated asset results in liability for owner.) **See also Moskowitz, supra, at 99-100.**

**4. Lessee Liability.**

CERCLA is not clear on the issue of lessee liability, since the statute is phrased in terms of "operators." 42 U.S.C. § 9607 establishes liability for:

(3) the . . . operator of a facility,

(4) any person who at the time of disposal of any hazardous substance . . . operated any facility at which such hazardous substances were disposed of . . .

Although liability for an active operator is clear, the section does not clearly define liability for a passive lessee. **See** discussion of the "due diligence" defense, **supra**. Again, Section 9607(b)(3) creates a defense if the release was caused solely by the act or omission of a third party, but the defense is not available if the release occurred in "connection with a contractual relationship." The term "contractual relationship," under section 9601(35)(A) includes "other instruments transferring title or possession . . . A lease generally transfers possession.

Arguably, therefore, a passive lessee may be required to establish the elements of a "due diligence defense," the same as required for a present owner. This defense would require proof that the transfer of possession occurred after disposal of the waste and the

lessee had no reason to know of the disposal. **42 U.S.C. § 9601(35)(A)**. **See also Rodburg, Landlord and Tenants in the Age of Environment, 3 Natural Resources & Environment, 10, 14 (Fall 1988). See also Moskowitz, supra, at 74-75.**

**5. Arranger Liability**

Section 107(a)(3) of CERCLA imposes liability upon persons who arrange for the disposal of hazardous substances that they own or possess. Presumably, the intent of this section is to impose liabilities on the "generators" of hazardous substances, notwithstanding the fact that they may not own the land upon which the hazardous substances are ultimately deposited. These persons are in the best position to control the disposition of hazardous substances and arguably to avoid the effects of allowing these substances to be released into the environment.

**6. Liability for Persons who Accept Hazardous Substances for Transportation**

Section 107(A)(4) of CERCLA imposes liability upon transporters. This liability provision is somewhat limited, as it applies only to those carriers who selected the destination for disposal of hazardous substances. Consequently, if the transporter transports the substances to a disposal site selected by the generator, the transporter does not incur liability. **42 U.S.C. § 9607(a)(4)**.

**F. Scope of Liability**

Under Section 107, a liable party is responsible for the following:

(d) All costs of removal or remedial action incurred by the United States or a state which are "not consistent with the national contingency plan ("NCP");

(e) Any other necessary costs of responses incurred by any other person "consistent" with the NCP; and

(f) Damages for injury to, destruction of, or loss of natural resources, including the reasonable costs of assessing such injury, destruction or loss.

Note the difference between (a) and (b) above. In an action initiated by the EPA or by the State, the defendant has the burden to prove that the costs incurred by the EPA or by the State were "inconsistent" with the NCP. **See United States v. Northeastern Pharmaceutical & Chem. Co., 810 F.2d 726 (8th Cir. 1986) cert. Denied, 484 U.S. 848 (1987).** In a private party cost recovery action, the plaintiff must prove, under (b) above, that the necessary costs of response were "consistent" with the NCP.[2] **See City of New York v. Exxon Corp., 633 F. Supp. 609 (S.D.N.Y. 1986).**

### H. Private Party Litigation

#### 5. Right of Contribution

Although the early decisions addressing private party contribution rights held that such a right existed under federal common law, **see United States v. Ward, 1984 WL 15710 (E.D.N.C. 1984)**, the language of section 107 seemingly makes such a common law analysis unnecessary. Section 107 provides that covered parties are liable for costs "incurred by any other person." **42 U.S.C. Section 9607(a)(4)(A). See City of Philadelphia v. Stepan Chem. Co., 544 F. Supp 1135, 1141-43 (E.D. Pa. 1982).** The 1986 SARA amendments, however, resolved any confusion on this issue. **42 U.S.C. § 9613(f)(1)** provides that "[a]ny person may seek contribution from any other person who is liable or potentially liable under section 9607(a)."

In the early years of CERCLA, some Courts held that a private party may recover costs from another only if the site was listed on the National Priority List. **See Cadillac Fairview v. Dow Chemical Company, 1984 WL 178617 (C.D. Cal. 1984)**. Other Courts expressed the more rational view that only some form of government approval is necessary before allowing a private party cost recovery action. **See Bulk Distributing Centers, Inc. v. Monsanto Co., 589 F. Supp. 1437 (S.D. Fla. 1984); Pinole Point Properties Inc. v. Bethlehem Steel Corp., 596 F. Supp. 283 (N.D. Cal. 1984).** The better view, however, appears only to require private parties to prove that the costs incurred were "consistent with" the NCP. **United States v. Northeastern Pharmaceutical & Chem. Co., 579 F. Supp. 823 (W.D. Mo. 1984); Amoco Oil Co., v. Borden, Inc., 889 F.2d 664 (5th Cir. 1989); Cadillac Fairview/California v. Dow Chemical Co., 840 F.2d 691 (9th Cir. 1988); Tanglewood East Homeowners v. Charles-Thomas, Inc., 849 F.2d 1568 (5th Cir. 1988); Roe v. Wert, 706 F. Supp. 788 (W.D. Okla. 1989)** (citizen suit requires 60-day pre-suit notice); **Wickland Oil Terminals v. Asarco, Inc., 792 F.2d 887, 890 (9th Cir. 1986); NL Industries, Inc. v. Kaplan, 792 F.2d 896 (9th Cir. 1986).**

**6. Extent of Contribution**

In apportioning liability among private parties for response costs, the Courts may consider a broad range of equitable factors under section 113(f). These factors are set forth in the legislative history of the amendment, and they include (i) the amount of the hazardous substances involved; (ii) the toxicity level of the hazardous substances; (iii) the degree of the parties' involvement in disposing of the hazardous substances; (iv) the level of care exercised; and (v) the degree of the parties' cooperation with federal, state or local officials.

**See H. Rep. No. 153, 99 Cong., 1st Sess. 18-19 (1985).**

Because a present owner of a facility is a person who may be liable for response costs under section 107, the issue of contribution often arises where the present owner, who arguably had nothing to do with the disposal of the contaminants, brings suit under CERCLA against the generators and transporters of the hazardous substances. In **Gopher Oil Co. v. Union Oil Company of California, 757 F. Supp. 988 (D. Minn. 1990)**, the Court allocated all of the liability for past and future response costs to the previous site owner. In **Gopher**, the present owner neither caused nor contributed to the contamination of the property. In **Weyerhauser Co. v. Koppers Co., 771 F. Supp. 1420 (D. Md. 1991),** the Court reached a different result on markedly different facts. The owner in **Weyerhauser** not only knew of and acquiesced in the disposal activities, but also had required them as a condition of the lease with the operator. Consequently, the Court reasoned that the owner had received some benefit from the operations, and apportioned the liability 40% to the owner and 60% to the operator. **See, e.g., United States v. A&F Materials Co., 578 F. Supp. at 1256; Amoco Oil Co. v. Borden, Inc., 889 F.2d at 672-73; United States v. Monsanto, 858 F.2d at 168 n.13.**

**7. Conditions Precedent to Private Action.**

Before initiating a claim under CERCLA, the party seeking cost reimbursement must have incurred at least one cognizable response cost. **See Trimble v. Asarco, 232 F.3d 946, 951 (8th Cir. 2000); Cook v. Rockwell International Corp., 755 F. Supp. 1468 (D. Colo. 1991). See also Alloy Briquetting Corp. v. Niagara Vest, Inc., 756 F. Supp. 713 (W.D.N.Y. 1991).**

### 8. Attorney's Fees.

The Supreme Court has addressed the question of whether attorney's fees are a "necessary cost of response" within the meaning of CERCLA § 107 (a) (4) (B) to resolve a dispute between the Circuits. **Key Tronic Corporation v. United States, 511 U.S. 809 (1994)**. Key Tronic brought suit against the Air Force for contribution of clean-up costs, including attorney's fees. The Court found no clear congressional intent to overcome the presumption that each party must pay its own costs in a recovery action. The Court distinguished between costs incurred in pursuing litigation in one party's interest, and those actions which relate directly to actual clean-up. The cost of identifying other responsible parties may be a reimbursable necessary response cost, even if the work is done by an attorney. **FMC Corp. v. Aero Industries, Inc., 998 F.2d 842 (10th Cir. 1993).**

## H. Approaching the Third Decade of CERCLA

In the 1980s and early 1990s, the federal Courts generally rejected all arguments against broad liability under CERCLA. As CERCLA enters its third decade, new trends can be gleaned from the judicial decisions. These trends are exemplified in a recent Supreme Court decision defining the breath of liability under Section 107, decisions narrowing liability from the passive migration of contaminants, and judicial efforts to resurrect the third-party defense under Section 107(b)(3).

### 1. Corporate Liability

In 1991, the United States District Court for the Western District of Michigan held that a corporate parent could be liable under CERCLA for contamination at a site owned and operated by a subsidiary. **See CPC International, Inc. v. Aerojet-General**

**_____, 777 F. Supp. 549 (W.D. Mich. 1991).** Focusing on the remedial nature of the statute instead of on the traditional corporate doctrine of limited liability, the District Court held that if a corporate parent exercises "power" or influence over its subsidiary by actively participating and exercising control over the subsidiary's business during a period of disposal of hazardous wastes, then the parent is directly liable under CERCLA. **Id. at 573**. After a decision by the Sixth Circuit, the Supreme Court granted certiorari to clarify the issue of corporate parent liability under CERCLA. **United States v. Bestfoods, 524 U.S. 51 (1998).**

In **Bestfoods**, the Supreme Court reverted to traditional notions of corporate limited liability by holding that a parent corporation that actively participates in and exercises control over the operations of a subsidiary may not be held liable as an operator of a contaminated site owned and operated by the subsidiary, unless the corporate veil is pierced under state law. The Supreme Court expressly found that CERCLA does not authorize a departure from traditional principles of limited liability for a corporate parent: "It is a general principle of corporate law deeply 'engrained in our economic and legal systems' that a parent corporation (so-called because of control through ownership of another corporation's stock) is not liable for the acts of its subsidiaries. . . . Although this respect for corporate distinctions when the subsidiary is a polluter has been severely criticized in the literature, . . . nothing in CERCLA purports to reject this bedrock principal, and against this venerable common law backdrop, the congressional silence is audible." **Id. at 1884-85.**

It is important to note that, in **Bestfoods**, the Supreme Court recognized that a parent corporation may be liable directly for its own acts where those acts satisfy the elements of

operator liability under CERCLA. **Id. at 1886.** However, the Court refused to sanction a broad interpretation of the statute which would place (i) direct CERCLA liability on a parent under circumstances where the parent is not a "operator" based on its own actions or (ii) vicarious liability under circumstances where the corporate veil could not be pierced by traditional veil–piercing standards. **Id. at 1885-87.** The Court refused to discard the notion that officers employed by both the parent and a subsidiary are presumed to serve the subsidiary when acting on behalf on the subsidiary. The Court explained "there would in essence a relaxed, CERCLA–specific rule of derivative liability that would banish traditional standards and expectations from the law of CERCLA liability." **Id.**

**2. Passive Migration**

In the late 1980s and the early 1990s, the majority of Courts that addressed this issue viewed passive migration of contaminants as a form of disposal under CERCLA. **See, e.g., Nurad, Inc. v. William E. Hooper and Sons, 966 F.2d 837, 845 (4th Cir.), cert. denied, 506 US 940 (1992); Stanley Works v. Snydergeneral Corp., 781 F. Supp. 659, 664 (E.D. Cal. 1990).** In **Nurad Inc.**, the Fourth Circuit reasoned that reading "disposal" to require "active participation" would frustrate CERCLA's policy to remedy environmental hazards. **Nurad, 966 F.2d at 845.**

The more recent decisions have retreated from such a broad reading of "disposal." Under current decisions, passive migration of contamination does not invoke CERCLA liability unless a party consciously acted to dispose of the waste or acted in a manner that promoted migration. **See, e.g., United States v. 150 Acres of Land, 204 F.3d 698, 704 (6th Cir. 2000);ABB Industrial Sys., Inc. v. Prime Tech, Inc., 120 F.3d 351, 358-59 (2nd Cir.**

**1997)**; **United States v. CDMG Realty Co., 96 F.3d 706, 713 (3d Cir. 1996); Kalamazoo River Study Group v. Rockwell Int.l, 3 F. Supp. 2d 799, 812 (W.D. Mich. 1998); Carson Harvard Village Ltd., v. Unocal Corp., 990 F. Supp. 1188 (C.D. Cal. 1997).**

In **ABB Industrial**, the Second Circuit held that prior owners and operators of a contaminated site were not responsible under CERCLA for the passive migration of chemicals that were already in the ground. In **CDMG Realty,** the Second Circuit determined that CERCLA's definition of "disposal" was not so broad as to hold a prior owner or operator liable for the passive migration of contaminants from a landfill. **CDMG Realty, 96 F.3d at 714.** The Court stated that rejecting liability for passive migration is consistent with CERCLA's goal to "force polluters to pay the costs associated with their pollution." That goal is not served if "a person [who] merely controlled a site on which hazardous chemicals have spread without that person's fault is liable as a polluter." **ABB Industrial, 120 F.3d at 358-59. See, also M. Chertok and M. Bogin, "Passive Disposal: New Protection Now Available" 218 N.Y.L.J. S2 (1997).**

**3. Resurrection of the Third-Party Defense**

Traditionally, the Courts have rejected a third-party defense for contaminants that were released during the period of the defendant's ownership of the site. In such a situation, the Courts generally concluded that, although the owner was not directly responsible for the tenant's actions, the release was not caused "solely by the acts or omissions of a third-party," and the defendant failed to take precautions against the foreseeable acts of others. **See**, **e.g.**, **New York v. Shore Realty Corp., 759 F.2d 1032 (1985)**.

In the mid and late 1990s, the Courts have been more receptive to the third-party defense. In **New York v. Lashins Arcade Co., 91 F.3d 353 (2nd Cir. 1996)**, the Second Circuit held that a shopping center owner was not liable under CERCLA for contamination from a dry cleaner that leased space years before the site owner had acquired the property. The Second Circuit held that the shopping center owner was protected by the third-party defense. In **Lashins Arcade Co.,** the State of New York argued that the shopping center owner was not entitled to the third-party defense because it had failed to adequately investigate the site, or to exercise "due care" regarding the contamination which existed. The Second Circuit rejected the State's arguments:

> It is surely the policy of CERCLA to impose liability upon parties responsible for pollution . . . rather than the general tax paying public, but this policy does not mandate precluding a "due care" defense by imposing a rule that is tantamount to absolute liability for ownership of a site containing a hazardous waste.

**Id. at 361-62.**

#### 4. Section 107 v. Section 113

During the early years of CERCLA, PRPs, such as a present landowner, often brought Section 107 actions against those who were culpable for the disposal of hazardous substances. These actions were based on the express language of Section 107, which clearly authorizes private parties to bring actions to recover response costs. **See 42 U.S.C. Section 9607(a)(4)(B).** In a private cost recovery action, the land owner assumed the position of the government and sought to hold arrangers, transporters, and past operators jointly and severally liable for all response costs incurred. **See Key Tronic Corp. 511 U.S. at 812 n 7.**

Judicial reception to private cost recovery actions has changed dramatically in the last five years. The question presented is whether a PRP may maintain a Section 107 "cost recovery" action, or whether the PRP must proceed with a "contribution" action under Section 113. Although there is a split of authority in the lower Courts, "every Court of Appeals that has examined this issue has come to the same conclusion: a section 107 action brought for recovery of costs may be brought only by innocent parties that have undertaken clean-ups," and a non-innocent PRP may only bring a section 113 action for contribution." **New Castle County v. Halliburton NUS Corp., 111 F.3d 1116, 1120 (3rd Cir. 1997)** (emphasis in original). The Tenth Circuit adopted this position in **United States v. Colorado Eastern R.R. Co.**, **50 F.3d 1530 (10th Cir. 1995)**. The First, Third, Seventh, Ninth, and the Eleventh Circuits have reached the same conclusion. **See Bedford Affiliates v. Sills, 156 F.3d 416 (2nd Cir. 1998); Pinal Creek Group v. Newmont Mining Corp., 118 F.3d 1298 (9th Cir. 1997); United Technologies Corp., v. Browning-Ferris Industries, Inc., 33 F.3d 96 (1st Cir. 1994), cert. denied., 513 U.S. 1183 (1995); Akzo Coatings, Inc. v. Aigner Corp., 30 F.3d 761 (7th Cir. 1994).** These Courts have found that the 1986 enactment of Section 113 indicates that Congress intended contribution to be an exclusive remedy for PRPs, that to allow PRPs to recover clean up costs under Section 107 would render Section 113 meaningless, and that the availability of Section 107 actions should be limited to governmental or "innocent PRP's for public policy reasons." **See, e.g., United Technologies, 33 F.3d at 100; Colorado Eastern R.R. Co., 50 F.3d at 1536**.

Despite the apparent trend to limit Section 107 actions by private parties, the claim has not been entirely extinguished. Section 107 historically has been used by the

government to recoup the costs incurred in investigating and responding to hazardous substances. Some courts have noted that allowing "any other person" – including a PRP – to bring a 107 action is consistent with the plain language and expressed goals of CERCLA because it provides PRPs with an incentive to effectuate a prompt clean-up. **See, e.g., Companies for Fair Allocation v. Axil Corp., 853 F. Supp. 575 (D. Conn. 1994); United States v. Kramer, 757 F. Supp. 397, 416-17 (D.N.J. 1991).** Thus, several district courts have held that PRPs that are "innocent" may maintain a direct 107 action. **See Rumpke of Indiana, Inc. v. Cummins Engine Co., Inc., 107 F.3d 1235, 1239-42 (7th Cir. 1997); Boyce v. Bumb 944 F. Supp. 807, 812 (N.D. Cal. 1996);**

"Innocent" in the context of CERCLA, appears to mean "parties who [are not] themselves liable" under CERCLA, i.e., those who can establish "innocent landowner" defense under Section 101 (35) and Section 107 (b). **See, e.g., United Technologies, 33 F.3d at 100; Redwing Carriers v. Saraland Apts., 94 F.3d 1489, 1513 (11th Cir. 1996)** ("parties who are not themselves liable or potentially liable for response costs under Section 107 (a) of CERCLA can bring a cost recovery action directly under Section 107 (a) against potentially responsible parties"). The Fifth Circuit however, has taken a more expansive view, recognizing that "it is possible that, although falling outside of the statutory parameters" of innocence, "a PRP who spontaneously initiates a clean-up without government prodding" may maintain a direct claim under section 107 (b). **See United Technologies, 33 F.3d at 99 note 8**.

The distinction between a section 113 and section 107 is of paramount importance. In a section 107 action, the plaintiff must establish a *prima facie* case, which includes only

satisfying the four elements of section 107 (a). Those elements are that: the defendant falls in one of the four categories of "responsible parties," hazardous substances were disposed of at a "facility," there was a "release" of hazardous substances into the environment, and the release caused "response costs to be incurred." **See 42 U.S.C. § 9607**. The burden then shifts to the defendant of proving that the harm at the site is divisible, and there is a reasonable basis for portioning liability for response costs. **See**, **e.g.**, **Kelley v. Thomas Solvent Co.**, **727 F. Supp. 1532, 1552 (W.D. Mich 1989)**. The practical consequence of placing this burden on defendants is that it becomes difficult to escape the joint and several liability.

In contrast, in a typical section 113 contribution action, the plaintiff must not only demonstrate that the defendant is a "covered person" under section 107, but also has the additional burden of proving each defendant's allocable share of damages. **See United States v. Taylor, 909 F. Supp. 355, 361 (M.D.N.C. 1995); United States v. Atlas Minerals and Chemicals, Inc., 1995 WL 510304 at *188 (E.D. Pa. 1995)**. A PRP's "defense" to a section 113 claim also differs from a defense to a section 107 claim. Under section 107, the defendant must prove a reasonable "apportionate of harm" to establish a divisibility defense to the imposition of joint and several liability. In section 113, a defendant simply cannot be "allocated" more than its "equitable share" of several liabilities for the harm at a site. **See United States v. Western Processing Co., 734 F. Supp. 930, 938 (W.D. Wash. 1990)**. Thus, even if a defendant cannot show a reasonable basis for apportioning the harm (which is a defense to a section 107 claim) a defendant in a section 113 contribution proceeding can rely on any number of "equitable factors" to allocate that defendant's proportionate share of response costs.

### 5. Limiting Liability for Passive Migration

In the CERCLA early years, a landowner could be liable as a "covered person" under section 107 if contaminants migrated through the groundwater and underneath her property. The majority of courts that addressed this issue viewed passive migration of contaminants as a form of "disposal" under CERCLA. **See, e.g., Nurad, 966 F.2d at 845; Stanley Works, 781 F. Supp. At 664.** In the latter half of the 1990s, courts have retracted the meaning of "disposal" and have held that passive migration of contamination does not implicate CERCLA liability unless a party acted in a manner which promoted the migration through the soil or groundwater. **See, e.g., ABB Industrial, 120 F.3d at 358-59; CDMG Realty, 96 F.3d at 713; 150 Acres of Land, 204 F.3d at 698.**

### 6. Restricting Lender Liability

Section 101 (20) of CERCLA includes a security interest holder exemption that excludes from liability those who, without participating in the management of a facility, hold "indicia of ownership" primarily to protect a security interest. **42 U.S.C. § 9601(20)**. The Eleventh Circuit in **United States v. Fleet Factors Corp., 901 F.2d 1550 (11th Cir. 1990), cert. denied, 498 U.S. 1046 (1991)**, caused considerable concern within the lending community by holding that a lender who has the ability to participate in the management of a business cannot avail itself of the exemption. Additionally, the exemption disappeared once the lender obtained title through foreclosure, since the lender now held title rather than an "indicia of ownership."

In response to the **Fleet Factors** decision, EPA issued a rule clarifying the scope of the security interest exemption to provide lenders with certain a safe harbor. **See 57 Fed.**

**Reg. 18,344 (April 29, 1992)**. This rule was immediately challenged in **Kelley v. EPA, 15 F. 3d 1100**, **reh'g denied**, **25 F.3d 1088 (D.C. Cir. 1994), cert. denied, American Bankers Association v. Kelley, 513 U.S. 1110 (1995)**. The D.C. Circuit vacated EPA's rule, holding that an administrative agency has no authority to issue regulations defining the liability under Section 107 of CERCLA. The Court declared that, when lenders are named as defendants under CERCLA, the "claim . . . should be evaluated by the federal courts independent of EPAs institutional views." **Id. at 1109.**

Congress responded to the invalidation of EPA's "safe harbor" rule by passing the Asset Conservation, Lender Liability and Deposit Insurance Protection Act of 1996 "ACA," 110 Stat. 3009–462. The law amended the secured creditor exemption of CERCLA and essentially validated EPA's lender liability rule. The ACA states that secured lenders who do not participate in management are not owners or operators within the meaning of CERCLA and therefore not liable for response costs. Additionally, the ACA provides that lenders may take certain actions prior to and after foreclosure without invalidating the secured creditor exemption. A lender may:

4. Sell, lease or liquidate the facility in question;
5. Maintain business activities or wind-up operations at a facility; or
6. Undertake response actions with respect to hazardous substance contamination.

The aforementioned activities are exempted only if the lender is actively attempting to divest itself of the facility "at the earliest practicable, commercially reasonable time, on commercially reasonable terms, taking into account market conditions and legal and

regulatory requirements." **42 U.S.C. § 9601(20)(E)(ii).**

The ACA also clarified the types of activities in which lenders may engage and not specifically "participate in management." These include:

1. Providing financial or administrative advice and assistance to the borrower;
4. Restructuring a loan agreement;
3. Possess the capacity to influence facility management, or the unexercised right to control operations;
4. Ensuring compliance with environmental terms of the loan agreement; and
5. Requiring environmental response actions to be undertaken by the borrower, or directly undertaking such actions itself.

## VI. REUSE OF ENVIRONMENTALLY IMPAIRED PROPERTY

### A. Brownfields

The EPA defines "Brownfields" as "abandoned, idled, under-used industrial and commercial facilities where expansion or redevelopment is complicated by real or perceived environmental contamination." **See Brownfields Economic Redevelopment Initiative (September of 1995)**. While many factors have caused investors to shy away from Brownfields properties, CERCLA created the essential risk associated with ownership of previously contaminated sites. As discussed in Part V above, CERCLA's liability scheme imposed liability for the costs of clean-ups on a number of classes of "responsible parties," including current owners and operators of a contaminated site who arguably had nothing to

do with the contamination. Against this backdrop, the unattractiveness of an old industrial or commercial site is readily understandable.

The EPA has expressly acknowledged that CERCLA has acted as a significant impediment to the development of Brownfield properties, which are often located in low income or other depressed areas. In order to address this problem, Congress has afforded protection to lenders under the Asset Conservation, Liability and Deposit Insurance Protection Act, also discussed in Part V above. However, the main focus of the EPA and of the States has been to encourage development without the risk of incurring unnecessary liability. The EPA has two primary mechanisms for the clarification and liquidation of potential liability, both of which are discussed below:

**3. Comfort letters**

The purpose of comfort letters is to provide prospective purchasers and others with the best, current information about the EPA's interest, or lack thereof, in a given site. These letters summarize data available to the EPA regarding a site and, importantly, summarize the federal government's past actions and future expectations with respect to response actions at the site. The EPA will not issue a comfort letter for any property unless there is a realistic perception or a probability of a prospective new owner incurring CERCLA liability. The EPA policy, which may be found on the EPA website, sets out four types of sample comfort/status letters:

a. A "no previous federal Superfund interest" letter advises party that there is no evidence of past Superfund interest or involvement with the site (in other words, the site is not in the CERCLIS database).

b. A "no current federal Superfund interest" may advise a prospective purchaser that this site has been deleted from CERCLIS or from the National Priorities List.

c. A "federal interest" letter advises the prospective purchaser that the EPA is responding, or plans to respond, to contamination at a site.

d. A "State Action" letter indicates that the State has primary responsibility for any activities at this site.

**4. Prospective Purchaser Agreements ("PPAs")**

In contrast to a comfort letter, a PPA provides actual resolution or liquidation of any legal liability that the prospective purchaser might incur. EPA issued its guidance on agreements with prospective purchasers of contaminated property on May 24, 1995, which states that PPAs are available only for sites where there has been, or where there realistically will be, a CERCLA response action. This standard is more restrictive than that which governs the issuance of comfort letters. The essence of a PPA is a covenant not to sue the new owner for pre-existing contamination, which is generally granted in exchange for appropriate consideration. The covenant not to sue also qualifies pursuant to section 113 (f) (2) of CERCLA, to protect the new owner from possible contribution actions by other PRPs.

The EPA guidance states that in consideration of granting the covenant not to sue, the EPA should receive a substantial benefit either in the form of a clean-up, or an indirect public benefit in combination with a reduced direct benefit to EPA. Prior versions of the guidance restricted the consideration to direct benefits of cash or clean-up work. However, the current guidance recognizes the considerable indirect benefit that can be realized from

Brownfields redevelopment, including the creation or retention of jobs, the development of abandoned or blighted property, the creation of conservation or recreation areas, or the improvement of public transportation or infrastructure.