

This Essay for the Masters of Environmental Studies Degree

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LOSS OF INNOCENCE: ENVIRONMENTAL
LIABILITY FOR THE UNSUSPECTING

BY
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ABSTRACT

This essay examines the environmental liability of owners of real property. The methodology employed is to look at the federal and state statutes pertaining to hazardous waste sites and then the pertinent case law. Based on these sources an analysis of liability is made. The first statute explored is the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA). Definitions, the liability scheme and defenses are addressed. CERCLA is then compared to the Superfund Amendments and Reauthorization Act of 1986 (SARA) for differences in definitions/ liability and defenses. Both the Washington State Model Toxic Control Act and the California Carpenter-Presley-Tanner Hazardous Substance Act are examined for differences from the federal law.

Judicial decisions are then reviewed with a focus on parties such as lenders and insurers who are not principals in real estate transactions. Liability is retroactive, joint, strict and liable. Responsible parties are liable for remediation, natural resources damages and the cost of environmental risk assessment. The analysis of liability reveals that owners and operators as well as former owners and operators of hazardous waste facilities are strictly liable with very limited defenses even **if** they had nothing to do with the pollution. In light of some very creative judicial

interpretations, lenders, successor corporations and insurers have also been found liable for cleanup.

At present the only viable defense to liability is the exercise of environmental due diligence in the form of an environmental site audit. This defense is still untested in court, and is not specifically defined in the statutes. A bill to be attached to the 1991 Superfund reauthorization will define site audits for the purpose of environmental due diligence. In the moving target of judicial interpretation and the muddy statutory language, there is some uncertainty about liability.

With liability unclear, the following policy issues emerge. Uncertainty may drive some business offshore. Further, the high transaction costs attached with SARA may put the U.S. at a competitive disadvantage with the European Community which has adopted a cooperative system for dealing with wastes rather than an adversarial one. Finally there is the question of equity. CERCLA purported to make the polluter pay. As it stands, the innocent are guilty as well. Is it fair to target the innocent in pursuit of a social goal? Hazardous waste cleanup is a national problem. The enormous costs should be spread more evenly around society.

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INTRODUCTION

In response to public outcry over the chemical emergency at Love Canal, Congress passed the Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA) in 1980. The Resource Conservation and Recovery Act of 1976 was designed to deal with hazardous wastes generated in the present, but did not address previously produced wastes. CERCLA was drafted to deal with the wastes from the past (Josephson 1986). CERCLA was a compromise hammered out by a lame duck Congress and ratified just as it adjourned. CERCLA shows the signs of its hurried birth, replete with ambiguities, interesting construction and confusing grammar (Glass 1987).

CERCLA established a Superfund to pay for cleaning up hazardous wastes when no responsible parties could be found. CERCLA also granted EPA wide powers to enforce the new law (GAO 1989). Two major goals emerge from the Act: to clean up hazardous waste sites and have the private sector pay the cost (Moskowitz 1989). Ostensibly the polluter should pay, but CERCLA was designed to ensnare as many liable parties as possible with the narrowest of defenses as the Superfund was woefully underfunded to clean up the nation's toxic waste sites (Summers 1990). Since many polluters could not be found, EPA looked for so called deep

pockets that could pay now and in the future (Hammers 1990). Judicial interpretation has been instrumental in widening the circle of liability. One need merely own a piece of contaminated property, and having had nothing whatever to do with the hazardous waste on the site, to be liable for the entire cleanup (Summers 1990)

My goal in this essay is to examine the state of liability for owners of real property under CERCLA, as amended. In so doing I shall look at the appropriate statutes and judicial interpretations. Of particular interest are those parties that are 'innocent' of polluting but are nevertheless liable for cleanup costs under CERCLA. The current state of liability and its implications are examined. The prospects for future liability under CERCLA are my final points. The conclusion is that there is great uncertainty as to the extent of liability, particularly for lenders and corporations. This issue is important because a degree of certainty is crucial for business decisions, and unfavorable environmental laws tend to foster a hostile and costly business climate that drives business offshore. In addition, it is inherently unfair to target the innocent to pay for the guilty.

The chapters are presented in an order representing a logical progression in the argument. The first

chapter examines state and federal statutes dealing with hazardous waste liability. Then follows a lengthy chapter detailing the judicial interpretations of the statutes. A brief chapter on the costs associated with CERCLA is next, followed by the conclusion. Environmental liability for real property owners is a complicated and important issue; it is my hope that it is clarified by this essay.

Methodology

The focus of this essay is the liability imposed by CERCLA and the implications of this liability. Liability for the purpose of this essay means imposition of financial responsibility for the cleanup of environmental degradation resulting from hazardous wastes. Federal and state statutes will be addressed as each potentially could invoke liability. The interpretation of the courts is crucial because the combination of statute and judicial interpretation indicates the actual state of liability.

The liability will be elucidated by examination of the appropriate statutes, beginning with CERCLA/SARA on the federal level. By looking at the pertinent definitions and sections, I will show the liability scheme and defenses set down by the Act and its Amendments. As the state laws can also invoke liability the Washington State Model Toxics Act and the California Car-

penter-Presley-Tanner Hazardous Substance Act will be analysed for differences from the federal legislation that pertain to the liability issue.

Relevant judicial interpretations of the law will be discussed. Important decisions regarding owners, corporations, lenders and insurers require scrutiny to see the legal landscape we live in. The reason for the review of case law is that the statutes are given life by their interpretation by the courts; the current state of liability derives from the hazardous waste legislation and legal precedent.

The analysis of liability then lies within the framework supplied by the statutes and the guidance given by the judiciary. From these twin sources I will ascertain the liability of the principals in real estate transactions: owners, buyers, and sellers. Figure 1 depicts the CERCLA liability scheme. The vertical axis shows the time frame of liability. The horizontal axis represents the progression of the essay beginning at the left and ending at the right. Not to be forgotten are other parties who may have liability such as lenders, successor corporations and Insurers. What are the trends in liability, what direction are we heading? What are the implications for Potentially Responsible Parties and indeed the country? These are the issues to be addressed.

Figure 1
CERCLA Liability Scheme

Time Frame	Party	Statute	Judicial Interpretation	1990 Liability
Before Dumping	Owner	Not liable	No cases	Not liable
During Dumping	Owner	Liable	Liable	Liable
During	Operator	Liable	Liable	Liable
During	Lender	Exempt	Uncertain	Uncertain
During	Insurer	Not liable	Uncertain	Uncertain
Intervening	Owner/knows about pollution	May be liable	Uncertain	Uncertain
Intervening	Owner/doesn't know about pollution	Not liable	Uncertain	Uncertain
Intervening	Lender	Exempt	Uncertain	Uncertain
Intervening	Insurer	Not liable	Uncertain	Uncertain
Present	Owner	Liable	Uncertain	Uncertain
Present	Operator	Liable	Uncertain	Uncertain
Present	Lender	Exempt	Uncertain	Uncertain
Present	Insurer	Not liable	Uncertain	Uncertain
Future	Owner	Liable	Uncertain	Uncertain
Future	Lender	Exempt	Uncertain	Uncertain

CHAPTER 2

THE STATUTORY BASIS OF LIABILITY

The purpose of this chapter is to establish through an examination of the appropriate statutes what the federal and state laws say about the environmental liability of the parties to real estate transactions. First CERCLA is examined for the basic conditions and definitions leading to liability: Potentially Responsible Parties must be responsible for a 'release' of a 'hazardous substance' from a 'facility'. Costs of liability and defenses are also covered. Then the changes in the law resulting from the Superfund Amendments and Reauthorization Act of 1986 are addressed, focusing on the changes in defenses to liability. To complete the section, the counterpart state Superfund laws of Washington and California are characterised for the differences from the federal law.

Liability under CERCLA

Liability under Section 107 of CERCLA is based on the 'release' of 'hazardous substances' at a 'facility'. Under CERCLA Section 101.9:

The term "facility" means (A) any building, structure, installation, equipment, pipe or pipeline (including any pipe into a sewer or publicly owned treatment works), well, pit, pond, lagoon, impoundment, ditch, landfill, storage container, motor vehicle, rolling stock, or aircraft, or (B) any site or area where a hazardous substance has been deposited, stored, disposed of, or placed, or otherwise come to be located; but does not include

any consumer product in consumer use or any vessel. (42 § USCA 9601.9, West Publishing 1989) .

Looking carefully at the language here, between Parts A and B the word 'or' is used suggesting that all of A is considered a 'facility' even without any hazardous waste being involved. While not clearly stated, it must be assumed that Congress intended that category A contain hazardous waste to be considered a facility . While subparagraph A is an extensive listing of specific examples, subparagraph B is encompassing in its sweep: if hazardous wastes are present, then it's a facility, excepting consumer products and vessels.

CERCLA Section 101.14 defines 'hazardous substance' as:

(A) any substance designated pursuant to section 1321(b) (2) (A) of Title 33, (B) any element, compound, mixture, solution, or substance designated pursuant to section 9602 of this title, (C) any hazardous waste having the characteristics identified under or listed pursuant to section 3001 of the Solid Waste Disposal Act [42 § USCA 6921] (but not including any waste the regulation of which under the Solid Waste Disposal Act [42 § USCA 6901 et seq.] has been suspended by an Act of Congress), (D) any toxic pollutant listed under section 1317(a) of Title 33, (E) any hazardous air pollutant listed under section 112 of the Clean Air Act [42 § USCA 7412], and (F) any imminently hazardous chemical substance or mixture with respect to which the Administrator has taken action pursuant to section 2606 of Title 15. The term does not include petroleum, including crude oil or any fraction thereof which is not otherwise specifically listed as a hazardous substance under subparagraphs (A) through (F) of this paragraph, and the term does not include natural gas, natural gas liquids, liquefied natural gas, or synthetic gas usable for fuel (or mixtures of natural gas

and such synthetic gas). (42 § USCA 9601.14, West Publishing 1989).

Most of the definition is in terms of other Acts or other Sections of CERCLA. Federal standards are based on hazard due to corrosivity, reactivity, toxicity and flammability. Petroleum products are specifically exempted from CERCLA liability. The petroleum exemption aside, substances that pose public health or environmental risks are subject to hazardous listing by the government (Nanney 1990).

The lists of hazardous substances maintained by state and federal agencies are constantly expanding. Many more compounds will surely be added (Nanney 1990). As CERCLA applies retroactively, any substance added to the hazardous list will be covered under the Act. This leaves the prospect of incurring Superfund liability in the future for a presently nonlisted compound very real indeed. The implication specifically is the danger for a Potentially Responsible Party of buying a property where certain categories of substances not currently considered hazardous are present. More generally, the significance is the uncertainty engendered by the expansive and retroactive nature of the Act, as there is no provision for grandfathering of substances not previously listed (See 42 § USCA 9601.14 as above).

The mere presence of a hazardous substance does not invoke liability; a 'release' or 'threatened re-

lease' must occur. CERCLA Section 101.22 defines

'release' as:

any spilling, leaking, pumping, pouring, emitting, emptying, discharging, injecting, escaping, leaching, dumping, or disposing into the environment (including the abandonment or discarding of barrels, containers, and other closed receptacles containing any hazardous substance or pollutant or contaminant), but excludes (A) any release which results in exposure to persons solely within a workplace, with respect to a claim which such persons may assert against the employer of such persons, (B) emissions from the engine exhaust of a motor vehicle, rolling stock, aircraft, vessel, or pipeline pumping station engine, (C) release of source, byproduct, or special nuclear material from a nuclear incident, as those terms are defined in the Atomic Energy Act... and (D) the normal application of fertilizer. (42 § USCA 9601.22, West Publishing 1989) .

This definition limits individuals in CERCLA cause of action for workplace releases as well as exempting vehicle emissions. Also excluded are nuclear incidents and fertilizers. EPA estimated that over 22 billion pounds of hazardous chemicals were 'released' into the environment in 1987 (EPA 1989). The enormity of this figure indicates in part the size of the problem, as well as the breadth of the definition.

Liability for 'releases' of hazardous substances extends to those EPA refers to as Potentially Responsible Parties (PRPs). Figure 1 on page 5 outlines the liability scheme for PRPs. Potentially Responsible Parties under CERCLA Section 107(a) include:

(1) the owner and operator of a vessel or a facility,

(2) any person who at the time of disposal of any hazardous substance owned or operated any facility at which such hazardous substances were disposed of,

(3) any person who by contract, agreement, or otherwise arranged for disposal or treatment, or arranged with a transporter for transport for disposal or treatment, of hazardous substances owned or possessed by such person, by any other party or entity, at any facility or incineration vessel owned or operated by another party or entity and containing such hazardous substances, and

(4) any person who accepts or accepted any hazardous substances for transport to disposal or treatment facilities, incineration vessels or sites selected by such person, from which there is a release, or a threatened release which causes the incurrence of response costs, of a hazardous substance... (42 § USCA 9607a, West Publishing 1989) .

The wording in subsections 1 and 2 is not consistent.

In subsection 1, 'owner and operator' are listed. Must one be both? Under subsection 2 comes those who 'owned or operated'. This type of ambiguity is common within the Superfund law. The courts must decide the intent and thus the application of the legislation (Peck 1989). The law does specify that all present owners are PRPs without evidence of fault. Innocent owners having no knowledge of hazardous waste disposal on their property are considered fully liable under CERCLA, as under subsection 1 ownership alone incurs liability. Former owners must have been associated with the site at the time of contamination to incur liability. The original law left intervening owners out of the liability scenario. Generators and transporters are off-site contributors and are beyond the

scope of this essay. At issue are owners and/or operators.

There are several parties to real estate transactions that could be considered owners or operators. The principals are the buyer and the seller. Then there is the lender, should one be required. All of these players have been found to be owners and/or operators under CERCLA. In a lease situation, it is possible to have different owners and operators, with the lessor the owner, and the lessee the operator. Lessees can even be owners in a sub-lease situation. Figure 1 illustrates the different stages of liability by party and time sequence.

Under CERCLA Section 101.20:

(A) The term 'owner or operator' means (i) in the case of a vessel, any person owning, operating, or chartering by demise, such vessel, (ii) in the case of an onshore facility or an offshore facility, any person owning or operating such facility, and (iii) in the case of any facility, title or control of which was conveyed due to bankruptcy, foreclosure, tax delinquency, abandonment, or similar means to a unit of State or local government, any person who owned, operated, or otherwise controlled activities at such facility immediately beforehand. Such term does not include a person, who without participating in the management of a vessel or facility, holds indicia of ownership primarily to protect his security interest in the vessel or facility. (42 § USCA 9601 West Publishing 1989) .

By this definition, any person who owns or operates a facility is covered. The definition of facility is

quite broad, and so by implication is the definition of owner. Further, an owner cannot abandon liability by walking away from the site and leaving it to the vagaries of foreclosure. The previous owner is still responsible rather than the government entity that acquires the property. In what is known as the security interest exemption, parties holding title as collateral against a loan are exempt from CERCLA liability. The Act does not make clear whether the exemption applies to lenders should they foreclose on a property (Alvino 1988). As we shall see, this determination is left to the courts.

The extent of liability for PRPs follows.

Potentially Responsible Parties:

... shall be liable for

(A) all costs of removal or remedial action incurred by the United States Government or a State or an Indian tribe not inconsistent with the national contingency plan;

(B) any other necessary costs of response incurred by any other person consistent with the national contingency plan;

(C) damages for injury to, destruction of, or loss of natural resources, including the reasonable costs of assessing such injury, destruction, or loss resulting from such a release. (42 § USCA 9607a West Publishing 1989) .

Removal under CERCLA can be characterised as an emergency or short term response to an imminent threat to the environment. Remediation is the result of a planning process attempting a long term solution to a toxic release (King 1988). Liability under this section

includes not only public sector costs, but actions of private parties as well. Natural resources damage claims are brought by the government as trustee for the public with a limit of \$50 million (Simons 1989). With the cost of cleaning up sites having risen to an average of \$20-30 million, the potential costs are tremendous (Klotz 1989).

The nature of liability under CERCLA is summarized in Figure 2. While the language was left out of the final bill, the courts have decided that CERCLA liability is retroactive and strict. That the contamination occurred before the enactment of the legislation is irrelevant (Glass 1987). The courts have held that the social goal of cleanup overrides other legal considerations, including retroactivity (Weber 1989). Strict liability implies that it is absolute; under CERCLA the defenses are very sparse, even for the innocent landowner (i.e., the owner having contributed none of the pollution and having no knowledge of the pollution). Owners claiming adherence to accepted standards of the past are not immune from CERCLA liability (Hitt 1989). Liability is joint and several, meaning all parties are individually liable for the entire cost of cleanup. In theory this means a party contributing one barrel out of a million could be charged for the whole remediation (Weber 1989).

Figure 2
Parameters of CERCLA Liability

STRICT	Fault not an issue; limited defenses
RETROACTIVE	Applies to all hazardous waste sites including those created before passage of the Act
JOINT & SEVERAL	Each defendant is liable for the entire cost of cleanup despite the size of contribution
UNENDING	No statute of limitations; continuing liability

CERCLA Section 107 b provides very limited defenses to liability:

There shall be no liability under subsection (a) of this section for a person otherwise liable who can establish by a preponderance of the evidence that the release or threat of release of a hazardous substance and the damages resulting therefrom were caused solely by-

- (1) an act of God;
- (2) an act of war;
- (3) an act or omission of third party other than an employee or agent of the defendant, or than one whose act of omission occurs in connection with a contractual relationship, existing directly or indirectly, with the defendant (except where the sole contractual arrangement arises from a published tariff and acceptance for carriage by a

common carrier by rail), if the defendant establishes by a preponderance of the evidence that (a) he exercised due care with respect to the hazardous substance concerned, taking into consideration the characteristics of such hazardous substance, in light of all relevant facts and circumstances, and (b) he took precautions against foreseeable acts or omissions of any such third party and the consequences that could foreseeably result from such acts or omissions; or (4) any combination of the foregoing paragraphs. (42 § USCA 9607b West Publishing 1989) .

With the God and War defenses unavailable to most PRPs, the Third Party defense was the only available relief under CERCLA. A Third Party defense entails showing that a party not connected with the defendant was actually responsible for the contamination. As written, the Third Party defense was of little use. Under the original Act, 'contractual relationship' was unclear, especially pertaining to real estate contracts. This meant it was difficult to show that a seller was a Third Party (Smith 1989). The Superfund Amendments and Reauthorization Act of 1986 (SARA) provided a measure of relief by defining the term 'contractual relationship'. This definition is the basis of the 'innocent landowner' defense. To qualify for this defense, the buyer must have had no knowledge of the contamination and also thoroughly inspected the property to ascertain its environmental condition (Peck 1989) .

Changes Wrought by SARA

After wrangling over the legislation for two years and battling with Reagan over the final provisions, the Superfund Amendments and Reauthorization Act (SARA) was passed by the Congress in 1986. This section deals with the changes in liability brought by SARA. Along with setting precise cleanup standards, SARA also addressed the liability issue of 'innocent landowners' (as described above) as well as 'almost innocent landowners'. 'Almost innocent landowners', those with no knowledge of contamination but who had not conducted an environmental inspection, could now be granted a 'de minimus' settlement, indicating only minor culpability (McDavid 1989). EPA at its discretion could now separate the major polluters from those only technically guilty (Steinway 1987).

In amending CERCLA, Congress sought to mitigate the extreme liability for innocent landowners under Section 107. The new definition of 'contractual relationship' provided new exemptions and the basis for a usable defense, as well as a new PRP:

The term "contractual relationship" ... includes, but is not limited to, land contracts, deeds or other instruments transferring title or possession, unless the 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 ...
(42 § USCA 9601.35 West Publishing).

Under SARA 'contractual relationship' does include real estate contracts and deeds except when the contamination occurred before the transaction. The definition goes on to require that the defendant did not know of the pollution. The PRP is thus required to investigate the past owners and uses of the property following 'good commercial or customary practice' before buying it in order to qualify for the defense. The court is instructed to take into account the price and ease of detectability of the contamination to determine whether the defendant should be allowed to use this defense. In addition, governmental bodies and those acquiring facilities by inheritance are exempted from Superfund liability under this definition.¹

Far from precise, the definition welcomes interpretation by the courts. The requirement of 'good commercial or customary practice' is quite broad, open to many interpretations. This indicates the importance of the judicial role in interpreting the Act. The conditions regarding price and detectability of contamination are made for litigation, as appraisal and environmental inspection are not exact sciences. The price issue does show a sensitivity to the plight of a buyer paying full market for tainted property, and conversely, that a low price could imply knowledge of a defect. EPA has been reluctant to go beyond very loose

guidelines, instead preferring for standards to evolve over time. To settle the uncertainty of what constitutes environmental due diligence for the purpose of the innocent landowner defense, Rep. Curt Weldon has introduced legislation that would define the term (Baker 1990) .

The above definition of 'contractual relationship' does address the question of intervening owners ignored by CERCLA. With the advent of SARA, disclosure became a key element for intervening owners not responsible for contamination. The new liability scheme is this: if a party owns contaminated property, knows about it, and does not disclose this fact upon transfer of the property, then the party is liable under CERCLA/SARA. If the party does disclose the contamination, he is not liable. If the party had no knowledge of the contamination, there is no liability (Glass 1987). Unlike most areas of the Act, In this case ignorance is a defense.

SARA did add an 'almost innocent' provision that could help those who do not qualify for the innocent landowner defense. Under CERCLA 122(g) (1) (B), a defendant could be granted a de minimus settlement if the PRP owns the facility but did not know of the contamination upon purchase or contribute to any release.² This defense is appropriate for parties that did not conduct appropriate inquiry into the environmental

condition of the property they purchased but had no knowledge of contamination. EPA guidelines will not completely absolve the landowner of liability, but this does represent some relief from strict liability. In exchange for a settlement and cooperation in the clean-up, EPA is authorized to enter into a covenant not to sue with the PRP (Civins 1990).

State Statutes

In order to deal with hazardous waste sites at the state level, many states now have their own Superfund laws. This allows state environmental agencies to initiate cleanups and pursue polluters. A comparison between CERCLA and the state statutes is important because while CERCLA applies in the entire nation, the state law applies in the specific state should the state take the lead on the cleanup action. If EPA is the lead agency at a site, CERCLA applies. If the state agency takes the lead the state statute is invoked. The statutes of California and Washington are compared to CERCLA, with the result that the Acts are very similar, with some minor differences (Nanney 1990) .

State laws regarding hazardous waste sites tend to follow the federal example of CERCLA/SARA. While CERCLA is not a paragon of clarity, it does offer the advantage of a decade of judicial interpretation (Mac-

Intyre 1989). The California Carpenter-Presley-Tanner Hazardous Substance Account Act is California's version of Superfund. The California Act actually refers directly to CERCLA for its definitions of liability and defenses to liability. The innocent landowner defense is identical to the federal example. Under the Act, liability is strict and expressly codified unlike the federal law. The California Act also explicitly relieves residential owners of liability unless the state proves the responsibility of the individual, a reversal of federal law (Nanney 1990) .

The Washington State Model Toxics Control Act of 1988 borrows heavily from CERCLA. Section 4 of the Act, which enumerates liability, is very similar to CERCLA Section 107. One key difference is in the definition of 'owner or operator'. The Washington Act's definition adds "any person with any ownership interest in the facility or who exercises any control over the facility." (WAC 70.105d.020 (6) (a) (1989)). This is important because it appears to obviate the corporate veil and expose even stockholders to liability (MacIntyre 1989). Corporate successor liability could thus be very extreme. The Washington Act's requirements for the innocent landowner defense are more stringent than the federal law. Instead of 'due care' as required by Section 107 of CERCLA regarding the handling of hazard-

ous substances, Section 4 of the Model Toxics Act requires 'utmost care', in legal terms a more stringent standard. It could be very difficult to prove 'utmost care' in court, greatly reducing the utility of the innocent landowner defense (MacIntyre 1989). The Model Toxics Act codifies strict, joint and several liability, which is instead implied in CERCLA (WAC 70.105D.040 1989) .

Whether state or federal law is applied depends on which agency takes the lead at the site, EPA or the state. The states do follow CERCLA, and even clarify some of the ambiguities in the federal law. The tendency for the states is to follow judicial interpretation of CERCLA, codifying what the courts expressed as the legislative intent of Congress. The statutes present a confusing and ambiguous picture of liability (MacIntyre 1989).

The courts have the thankless job of making sense of the compromise that is CERCLA. One court complained:

...numerous important features were deleted during the closing hours of the Congressional session... The courts are once again placed in the undesirable and onerous position of construing inadequately drawn legislation. (US vs Northeastern Pharmaceutical & Chem, 579 F. Supp. 823, from Peck 1989) .

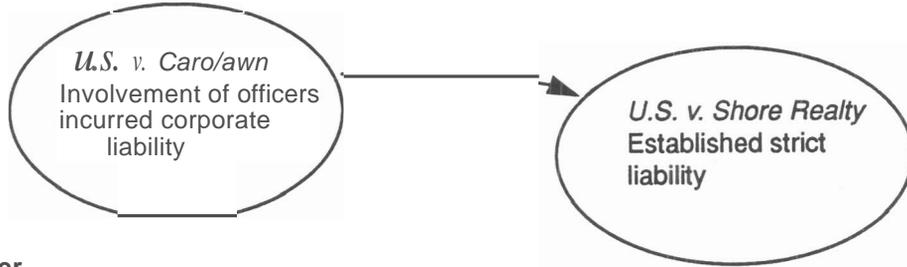
It is to the courts we now turn for clarification.

CHAPTER 3
JUDICIAL INTERPRETATION

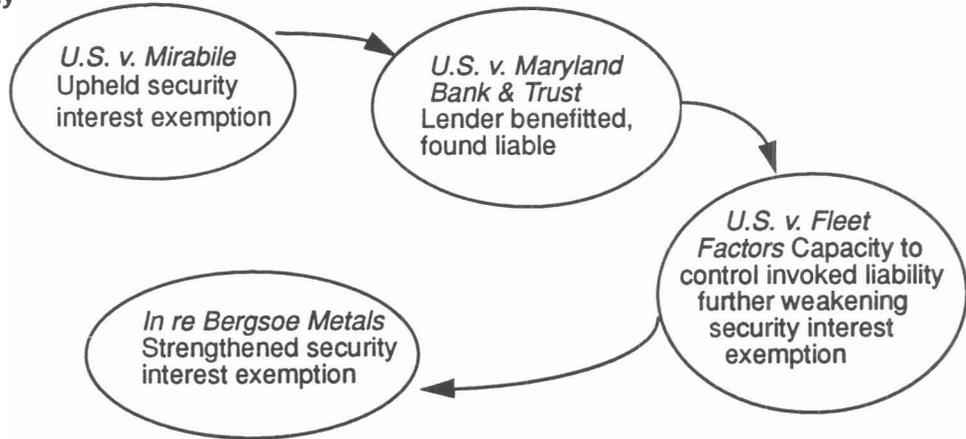
With CERCLA enacted, it fell to the courts to give it meaning. The courts could either strictly interpret the Act, or broaden the interpretation in the belief that this more closely followed the intent of Congress. The tendency has clearly been for a broad interpretation. The courts have gone beyond the letter of the law to assign liability to those able to pay, banks and corporations (Glass 1987). As this is relatively new legislation, the Judicial review is somewhat scanty. The following cases are presented because of their influence as evidenced by their repeated appearances in law journal articles on the subject of CERCLA liability. The cases examined are divided into sections as follows: early decisions affecting liability, lenders as owners, lessor/lessee liability, corporate successor liability, the innocent landowner defense and finishing with a summary of liability. Figure 3 summarizes the judicial decisions that are reviewed. The figure is a flow chart of the cases examined in the chapter with the horizontal axis representing liability increasing from left to right.

Figure 3
Flow Chart of Judicial Decisions
Relating to CERCLA Liability

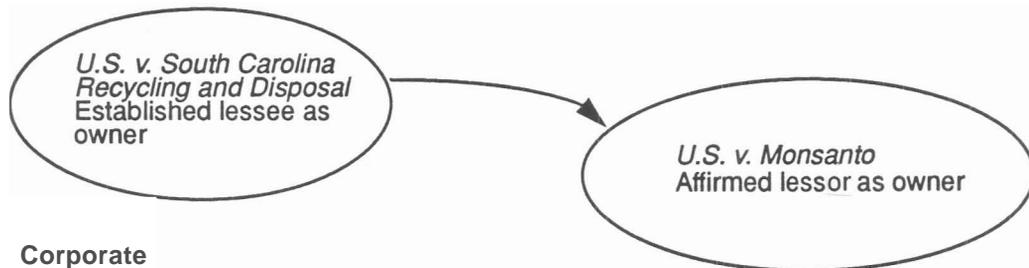
Early Decisions



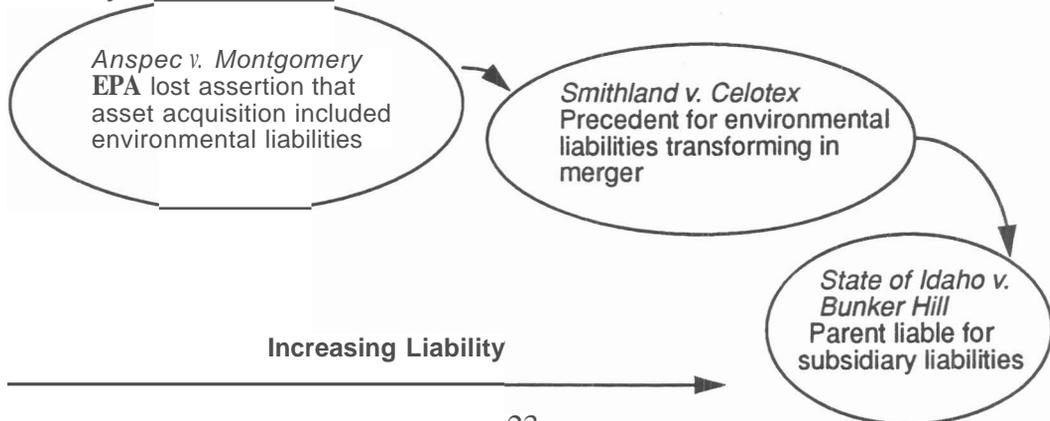
Lender Liability



Lessor/Lessee Liability



Corporate Successor Liability



Increasing Liability →

Early Decisions

An early case indicating the direction of judicial interpretation of CERCLA was *U.S. v. Carolawn* in 1984. The finding was that a corporation being used as a go-between in the sale of a waste dump was fully liable for cleanup under CERCLA even though it held title for a mere hour. The site, owned by the bankrupt Southeastern Pollution Control Company, was sold to Columbia Organic Chemical Company on June 2, 1976. Title was immediately signed over to three principals of Columbia Organic. Columbia Organic subsequently sought relief from liability as an owner of the site. The court held Columbia Organic liable with the admonition that holding "...title, or lack thereof, is not necessarily dispositive ... of ownership or control." (Env. Law Inst. 1984 from Summers 1990). In fact the court viewed Columbia Organic as an operator of the site because of the personal involvement of Columbia officers in hazardous disposal on-site. This interpretation was a precursor to the tendency of the courts to search beyond record of title to practice and intent in widening the circle of liability (Summers 1990).

The accepted precedent for strict liability for landowners under CERCLA is *New York v. Shore Realty* (Hayes 1990). Shore Realty purchased a waste site intending to develop it. Shore not only was aware of

the pollution, but in addition let the tenants remain and utilise the facilities and store more toxics on the site. The state sued Shore and a principle stockholder for cleanup costs. Shore argued that it was not responsible under Section 107(a) (1) of CERCLA as it neither owned the site when the release occurred or caused the release. The court disagreed, stating the opinion that CERCLA "unequivocally imposes strict liability on the current owner of a facility... without regard to causation." (759 F.2d 1044 (2nd Cir. 1985) from Summers 1990). The court added further:

...Shore's arguments would open a huge loophole in CERCLA's coverage...If the current owner of a site could avoid liability merely by having purchased the site after chemical dumping had ceased, waste sites certainly would be sold, following cessation of dumping, to new owners who could avoid liability otherwise required by CERCLA. Congress had well in mind that persons who dump or store hazardous waste sometimes cannot be located or may be deceased or judgement-proof. (759 F.2d 1045 (2nd Cir. 1985) from Summers 1990).

The court thus decided Congress' intent and held for strict liability. The key is that owners and operators are liable; how then do the courts decide the question of ownership?

Lenders as Owners

As previously discussed, CERCLA exempts from liability parties holding title for the purpose of protecting a security interest in property. The case law indicates that there is great uncertainty for

lenders in the courts. If a lender forecloses on a property, does it then become an owner liable under CERCLA? (Ditto 1989). The interpretation of the courts is of course crucial to this question. An early test case was *In Re T.P. Long Chemical Inc.* Long Chemical filed for bankruptcy. BancOhio held a perfected security interest in Long's personal property, which included drums of chemicals. The bankruptcy trustee sold everything except the drums, some of which were buried on the site. An above ground tank spilled and EPA responded and cleaned up the site. EPA then sought to recover its costs from the bankrupt estate and BancOhio. The court found the estate liable, but BancOhio was dismissed (King 1988). First, BancOhio did not benefit from the cleanup, as its interest was in personal property that did not increase in value as a result of the cleanup and had been sold previously anyway. Since BancOhio did not participate in the management of the facility, the court found that it "sought primarily to protect its security interest." (45 Bankr. 288-9 (Bankr.N.D. Ohio 1985) from Moelis 1990). BancOhio thus retained its security exemption.

U.S. v. Mirabile was a complex case involving three lenders and two owners. Turco Coatings was a paint factory repossessed by American Bank and Trust in 1981. American Bank and Trust sold the plant to the

Mirabiles four months later. EPA then informed the Mirabiles that the toxics on-site must be cleaned up. Finally EPA cleaned up the site and then sued the Mirabiles to recover the costs (King 1988). This led the Mirabiles to sue American Bank and Trust and the Mellon Bank, another lender of Turcos. American Bank and Trust and Mellon then sued the Small Business Administration, which had also lent money to Turco. The Mirabiles wanted American Bank and Trust and Mellon as fellow PRPs, while the banks wanted the Small Business Administration named as an operator as well (Ditto 1989) .

The court then had to rule on which parties were liable as owners and/or operators of the site. Though American Bank and Trust had actually held title to the property, the court found its actions consistent with maintaining its security interest. Because it did not participate in the operations of the plant, American Bank and Trust was absolved of liability (Hammers 1990). The court found that the Small Business Administration was mandated to participate in the management of its clients; further, it was not clear that the SBA had ever been involved in Turco's operations, so the SBA was also dismissed (Alvino 1988). Mellon Bank was not so fortunate. Mellon had participated in Turco's operations and one of its officers was closely involved

at the plant. The court allowed the Mirabile's suit against Mellon (King 1988). The decision in this case was a warning to lenders to take care not to become too involved in operations as opposed to the financial aspects of a borrower's business, but it is unclear just how far a lender may go without incurring liability (Ditto 1989).

The question of ownership liability arose again in *U.S. v. Maryland Bank and Trust*. Here the question was whether the security interest exemption held even when the lender continued to own the property after foreclosure. Maryland Bank and Trust foreclosed on the McLeod family dump site after loaning the son the money to buy the operation from his father. Maryland Bank and Trust took title to the property in 1982. In 1983 EPA informed Maryland Bank and Trust that the property was contaminated and would have to be remediated. Upon Maryland Bank and Trust's refusal to comply, EPA undertook remedial efforts and then sued the bank to recover cleanup costs (Moelis 1990, King 1988). Maryland Bank and Trust still owned the property when the court decision came down in 1986. Maryland Bank and Trust claimed it should receive the same exemption as American Bank and Trust had in the Mirabile decision. The court did not agree. Since the bank had benefitted

from the cleanup and continued to hold title, it was liable for the costs incurred by EPA (Hammers 1990).

The Maryland Bank and Trust case also confirmed the doctrine of joint and several liability, as the bank was held completely liable despite the fact it contributed none of the toxic contamination (Laseter 1990). Also addressed was the question of the confusing construction in Section 107(a) of CERCLA where subsection 1 requires the PRP to be an owner and operator while subsection 2 calls for owner or operator. In its defense the bank claimed in order to be held liable it must be both an owner and an operator of the facility. The court found that:

notwithstanding the language 'the owner and operator,' a party need not be both an owner and operator to incur liability under this subsection...The structure of section 107(a) of this hastily patched together compromise Act, is not a model of statutory clarity. It is unclear from its face whether subsection (1) holds liable both owners and operators or only parties who are both owners and operators...But by no means does Congress always follow the rules of grammar when enacting laws of this nation. (632 F. Supp. 573 (D. Md. 1986) from Glass 1987).

The court gave a broad interpretation based on the somewhat spotty legislative history. One need be only an owner or an operator to be found liable and need not have caused the hazardous release (Glass 1987).

With the Mirabile and Maryland Bank and Trust decisions at odds over the lender's security exemption, the financial community awaited judicial guidance as to

the state of liability. Two 1990 decisions served to further confuse the issue. *u.s. v. Fleet Factors* greatly expanded lender liability. Conversely, *In Re Bergsoe* came down for the security interest exemption.

The long awaited decision in *u.s. v. Fleet Factors* was announced on May 23, 1990. The Eleventh Circuit Court of Appeals handed down a decision on the extent of a creditor's involvement in a borrower's operations. Fleet Factors had agreed with Swainsboro Print Works to lend operating capital in exchange for Swainsboro's receivables. In addition, Fleet received a security interest in Swainsboro's inventory, equipment and site. Swainsboro filed for bankruptcy in 1979. Fleet continued with the advances, but also became involved in Swainsboro's operations as well as controlling access to the site (Berz 1991). In 1981, Swainsboro shut down. A trustee was appointed to take control of the facility. Fleet Factors foreclosed on its interest in the inventory and equipment in 1982 and engaged a liquidator to handle the matter (Moelis 1990). The liquidator moved hundreds of barrels of hazardous chemicals and allegedly caused the release of friable asbestos into the environment. An EPA inspection in 1984 revealed the presence of the chemicals and asbestos that posed a dangerous environmental risk. EPA cleaned up the site and then sued Fleet Factors as both

"owner and operator" under CERCLA Section 107 (a) (1) and an "owner or operator" under Section 107(a) (2) to recover the \$400,000 cleanup cost (Berz 1991). In the meantime, Emanuel County took title to the property at tax foreclosure (Moelis 1990).

The Federal District Court found that Fleet Factors was not liable under Section 107(a) (1) because it did not "own, operate or otherwise control activities at the facility immediately before the tax foreclosure." (724 F. Supp., 960 (SD Georgia 1988) from Moelis 1990). Further, the court decided Fleet Factors was not liable under 107(a) (2) as an "owner" because it was not involved in management of the facility. The issue of whether Fleet was an "operator" because of the movement of the drums and asbestos was left undecided and the case went to the 11th Circuit Court of Appeals. The Appeals judge upheld the lower court's ruling and agreed that the issue of the hazardous wastes and asbestos must still be decided. The Eleventh Circuit disagreed with the interpretations of CERCLA made by the lower court. The lower court had followed *Mirabile* in requiring a high standard of proof of involvement with management to trigger CERCLA liability. The Appeals Court instead made a sweeping expansion of the scope of liability by citing "capacity to control" rather than actual control (Berz 1991).

The court held that a lender could be held liable as a former owner:

by participating in the financial management of a facility to a degree indicating a capacity to influence the corporation's treatment of hazardous wastes... a secured creditor will be liable if its involvement with the management of the facility is sufficiently broad to support the inference that it could affect hazardous waste disposal decisions if it so chose." (901 F.2d 1550 (11th Cir. 1990) from Berz 1991).

This decision invoked liability surpassing *Maryland Bank and Trust*. The lender did not need to be involved in operations, but merely have the implied ability to control management decisions, to incur liability (Moelis 1990). The expansion of lender liability indicated by *Fleet Factors* sent shock waves through the banking community. After years of doubt because of the tension between the *Mirabile* and *Maryland Bank and Trust* decisions, *Fleet Factors* appeared to be a signal that the secured interest exemption was of very dubious utility (Berz 1991).

In August 1990, the Ninth Circuit Court of Appeals provided some relief with the ruling on *In Re Bergsoe Metal*. The Ninth Circuit rejected the "capacity to control" doctrine of *Fleet Factors*. The court instead followed *Mirabile* in finding that a lender foreclosing "primarily" to protect a security interest was not liable under CERCLA 107 (a) (1) or 9607 (a) (2) (Moelis 1990) .

In Re Bergsoe Metal involved a lead recycling facility that was financed by municipal bonds issued by a port authority. Bergsoe Metal Corporation was owned by a consortium headed by East Asiatic Company. The Port of St. Helens Oregon, sold fifty acres to Bergsoe on which to build the plant, Bergsoe sold the land back to the Port, and the Port assigned the lease back rights to US Bank of Oregon while the bank bought the Port's bonds. After the complex transaction was completed in 1981, the Port held the deed, and the Bank held a first trust position on the facility (Moelis 1990, Berz 1991).

After starting up in 1982 Bergsoe began having cash flow problems. A workout agreement whereby Front Street Management Corporation took over operations also faltered. The plant shut down in 1986 and the Bank forced Bergsoe into bankruptcy. At this point the Department of Environmental Quality concluded that the site was an environmental health hazard and the bank sued Bergsoe's owners, the East Asiatic Company demanding they take responsibility for the cleanup (Moelis 1990). East Asiatic Company countered back against the Bank as well as filing a third party claim against the Port, claiming the Port was liable as "owner or operator" under CERCLA. The Port argued that it owned the property only as security in the arrangement with

Bergsoe and that it did not participate in management. The court agreed and dismissed Bergsoe's claim (Berz 1991) .

Essentially the court held that the Port's rights under the sale/lease back deal with Bergsoe did not constitute "owner or operator" status under CERCLA. Under the net lease agreement, Bergsoe was responsible for the property. The Port did own the property on paper, but was not responsible in the sense of paying taxes and insurance (Moelis 1990). The court also found that the Port's rights of inspection and foreclosure under the lease did not constitute management, but instead were consistent with the rights of secured creditors (Berz 1991). For the Ninth Circuit, "Merely having the power to get involved in management, but failing to exercise it, is not enough [to incur liability.]" (In Re Bergsoe Metal Corp. No. 89-35397, 8637-8 no. 3 (9th Cir. Aug. 9, 1990) from Moelis 1990).

The status of lender liability has come full circle from *Mirabile* to *In Re Bergsoe Metals* with the intervening *Maryland Bank and Trust* and *Fleet Factors* cases, as seen in Figure 3. *Mirabile* and *Bergsoe* both strengthened the security interest exemption, while *Maryland Bank and Trust* and *Fleet Factors* expanded liability. *Fleet Factors* and *Bergsoe* are in direct conflict, *Fleet Factors* requiring only the broad capac-

ity to control while *Bergsoe* requires evidence of actions indicating control in order to incur liability. With these cases in opposition, lenders face an uncertain fate in the courts should they become embroiled in litigation over hazardous waste site liability.

Lessor/Lessee Liability

While it is obvious that lessors are owners and therefore liable under CERCLA, lessees have been found to be owners as well. (Of course lessees can also be operators.) In *U.S. v. South Carolina Recycling and Disposal*, Columbia Organic Chemical Co. leased a site for storage of chemicals and then sublet to South Carolina Recycling which also stored chemicals at the site. South Carolina Recycling took over the site and continued to store chemicals there. Ultimately a large amount of hazardous chemicals were dumped on the property and EPA cleaned the site and then sued Columbia and South Carolina Recycling for the costs. Columbia was judged an owner under CERCLA because it:

maintained control over...the property and, essentially, stood in the shoes of the property owners...To conclude otherwise would frustrate Congress' intent that persons with responsibility for hazardous conditions bear the cost of remedying those conditions. (653 F. Supp. 1003 (DSC 1984) from Feder 1988).

Control was thus equated with ownership. In *U.S. v. Monsanto* the court found that Monsanto as lessor was still liable as owner even though it had no knowledge

of the contamination occurring. (Prescott 1990) Because of the 'contractual relationship' clause in CERCLA, neither lessors nor lessees can easily use the innocent landowner defense (Feder 1988).

Corporate Successor Liability

The doctrine of limited liability that has been the basis of corporate planning throughout the industrialisation of America is under attack in the courts (Cross 1990). This is a very complex issue that delves into legal theories of corporate responsibility beyond the scope of this essay. Yet the importance to business of the corporate veil cannot be understated. The desire of the EPA to obviate corporate protection as a matter of policy strikes at the heart of u.S. business practices and engenders uncertainty. This has only become a concern in the past decade with the advent of CERCLA. Despite the established principle that in an asset acquisition the purchaser is not acquiring the seller's liabilities, EPA has taken the position that often environmental liability attaches despite deal structure. The EPA is thus asserting that environmental liabilities are in a different class and merit special treatment. EPA lost this assertion in *Anspec v. Montgomery* when the court held that CERCLA does not define successor corporations as PRPs. Conversely, in cases involving mergers the government has been very

successful in arguing for liability for successor corporations (Moskowitz 1989).

The precedent for mergers and the subsequent fate of attendant environmental liabilities was *Smith Land & Improvement v. Celotex Corporation*. In this case the court did not insist on CERCLA successor liability but noted that the intent of CERCLA was served by having the corporation pay (Squire 1990). The decision read in part:

...when two corporations merge pursuant to statutory provisions, liabilities become the responsibility of the surviving company...Congressional intent supports the conclusion that, when choosing between the taxpayers or a successor corporation, the successor should bear the cost. Benefits from use of the pollutant as well as savings resulting from the failure to use non-hazardous disposal methods inured to the original corporation, its successors, and their respective stockholders and accrued only indirectly, if at all, to the general public. (851 f.2d 86 (8th cir. 1988) from Cross 1990) .

The logic invoked in this case has had an extensive following in other court decisions. The courts have not been reticent to ignore the machinations of corporations reshuffling into new forms and still impose liability upon the successor (Squire 1990).

A case that addressed the question of responsibility of a parent corporation for the liabilities of a subsidiary was *State of Idaho v. Bunker Hill*. To be free of liability, the entities must operate independently and truly be at arm's length. The court used a

capacity to control test to determine if the parent, Gulf Oil, was liable. The court found that:

Gulf was in a position to be, and was, intimately familiar with hazardous waste disposal and releases at the Bunker Hill facility; and had the capacity to control such disposal and releases; and had the capacity, if not total reserved authority, to make decisions and implement actions and mechanisms to prevent and abate the damage caused by the disposal and releases of hazardous wastes at the facility...approval from Gulf was necessary before more than \$500 could be spent on pollution matters...With respect to Congress's intent that those who bore the fruits must also bear the burdens of hazardous waste disposal, it must be noted that Bunker Hill's authorized capital was a mere \$1100 (sic) while Gulf received \$27 million in dividends from Bunker Hill. Gulf fully owned Bunker Hill. (635 F. Supp. 665 (D. Idaho 1986) from Cross 1990).

While warning that normal transactions between parent and subsidiary corporations should not be misconstrued or twisted to the aim of invoking liability for the parent, in this case the evidence of control was so clear, the benefit so great and behaviour of the parent so egregious that Gulf was found fully liable for the cleanup (Alvino 1988). The courts are clearly finding reasons to pierce the corporate veil and assign liability to guilty parties.

Innocent Landowner Defense

To invoke the innocent landowner defense, the PRP must have exercised environmental due diligence in the form of an environmental site audit and have been unaware of the toxic contamination. The case law regarding the innocent landowner defense is still very

scant/ as this defense is quite new and site audits a recent addition to the process of closing a real estate transaction. In *International Clinical Labs v. Stevens*/ the buyer of a contaminated property brought suit against the seller/ the corporate lessee and the president of the corporation. The buyer was found to have had no knowledge of the pollution before the sale/ and have no part in any subsequent release. The defendants were found liable for a long term release at the site/ where computer hardware was manufactured/ and were fully liable for response costs. The buyer was absolved from liability under CERCLA Section 107(b) (3) despite the lack of an environmental site assessment because the evidence was overwhelming that the defendants were responsible for the release (Hayes 1990). No true test of environmental due diligence has yet been tried in court/ principally because it is a new concept (Baker 1990)

Summary of Liability

While the decisions rendered by the courts have been inconsistent/ some guiding principles emerge. First/ of overriding concern is the issue of control. If a party has control of a facility/ then liability is incurred. The difficulty is in ascertaining how much control must be exerted to be liable. The decisions are contradictory on this point/ as evidenced by *Fleet*

Factors and *Bergsoe*. Second, there is the intent of Congress. The courts have consistently found that Congress' intent was for the private sector to pay for cleanup, and have decided cases on that basis and gone beyond the strict letter of the law, as in *Smith Land*. Clearly the tendency has been for an expansion of liability as serving the intent of the Act. Finally, benefit has been a crucial factor. Parties seen to have benefitted from the pollution as did Gulf Oil In the *Bunker Hill* case or subsequent cleanup such as Maryland Bank and Trust, were found fully liable.

With limited defenses, the owner of real property where hazardous substances are found is strictly liable for the costs of investigating and cleaning up the site, as indicated in *u.S. v. Shore Realty*. These costs are now averaging from \$20-30 million per site. Under SARA, owners who disregard an order to clean a facility are also liable for treble damages (Civins 1990). Owner liability is summarized in Figure 4. Liability under CERCLA is retroactive, affecting past as well as present owners. Past owners are liable if they owned the property at the time of disposal, or knew of the contamination and sold the property without disclosure (Alvino 1988). Intervening owners with no knowledge of the pollution are not liable, seemingly the only parties with connection to the site in that

Figure 4
Owner Liability under CERCLA/SARA

Owner at time of dumping	Fully liable
Intervening owner/ didn't know of contamination	Not liable
Intervening owner/ knew of contamination, disclosed upon sale	Not liable
Intervening owner/ knew of contamination, didn't disclose	Fully liable
Present owner, knew of contamination	Fully liable
Present owner, didn't know of contamination, no due diligence	Could be liable
Present owner, didn't know of contamination, practiced due diligence	Very likely not liable

position (Civins 1990). EPA considers lessees to be owners even though the courts have found lessees to be owners only in cases where they have sublet the site as in *u.s. v. South Carolina Recycling and Disposal*.

Lessors are considered owners under CERCLA and are liable for contamination caused by their lessees, as demonstrated in *New York v. Shore Realty* and *u.S. v. Monsanto*. Lessees still remain liable as operators and may be sued in private action by their landlords. Lessees are considered operators when involved with a hazardous waste facility (Feder 1988). The situation becomes complicated by any pre-existing pollution on the site. Both lessor and lessee are considered PRPs in this case. Despite any contractual agreement with the lessee, the lessor is still responsible as owner (Glass 1987).

Despite the security interest exemption delineated in CERCLA, lenders who foreclose have been found to be owners under the Act as in *u.S. v. Maryland Bank and Trust*. Clouding the issue is the decision in *u.S. v. Mirabile* granting the bank its security exemption (Berz 1991). More chilling for lenders is the prospect of being held liable as an operator of a facility for exercising too much control over a borrower's business. The extreme example of this is the 1990 decision in *u.S. v. Fleet Factors* where capacity to control was

deemed sufficient to give operator status to the lender. *In re Bergsoe Metal* however came to the opposite conclusion about management participation and read a narrower construction of CERCLA (Moelis 1990).

For corporations the liability issues focus on officers, successor corporations and parents of environmentally unsound subsidiaries. As demonstrated in *U.S. v. Carolawn*, officers can be held personally liable if directly responsible for operations. Corporate law exempts successors from the liabilities of predecessors with certain exceptions (Cross 1990). In cases such as *Smith Land & Improvement v. Celotex Corp.* the courts have expanded corporate liability to further the legislative aims of environmental cleanup paid for by the polluter and held successors liable. Where parent corporations have been clearly involved with the subsidiary such as *State of Idaho v. Bunker Hill*, the parent has been held strictly liable as owner. While the courts have followed successor rules to a point, the application has been uneven with resulting uncertainty in the business community (Squire 1990). The tendency has been to expand liability with many corporations unaware of this potential exposure (Barnard 1987).

A law as confusing and contradictory as CERCLA desperately needs clarification from the courts. Yet

the expansion of liability afforded CERCLA by the courts is beyond rational application of the law and instead looks to banks and corporations as parties capable of footing the enormous bill for toxics cleanup (Glass 1987). Indeed, the *Fleet Factors* court cited the "overwhelmingly remedial goal of the CERCLA statutory scheme," and argued that "ambiguous statutory terms should be construed to favor liability for costs incurred by the government." (901 F.2d 1550 (11th Cir. 1990) from Hayes 1990). The implications of this expansive view of liability follow.

CHAPTER 4
IMPLICATIONS OF LIABILITY

Clearly there are costs attached to the liability resulting from CERCLA. This chapter explores the effects on the parties to real estate transactions. Always the uncertainty for business is of paramount concern, particularly for lenders. The attempt of business to shift the burden of cleanup costs to the insurance industry and the resulting battle is then examined. Finally, recommendations are made regarding defenses and protections the various parties can avail themselves of.

Costs of Liability

Buyers, sellers and lenders all face potentially huge transaction costs as a result of the spectre of Superfund liability. The primary costs are for legal fees and environmental audits. At present the only affirmative defense to liability is the innocent landowner defense under which the purchaser undertakes environmental due diligence in the form of a site audit (Baker 1990).³ The buyer requires the site audit in order to qualify for the innocent landowner defense. The potential liabilities of past owners indicates that sellers should take great care to know the condition of their property lest greater environmental damage be caused by the buyer which the seller could be liable

for. Sellers also may be liable to private cause of action, meaning that the buyer or other affected citizens could sue for damages resulting from environmental degradation (Hayes 1989).

As a result of the uncertainty surrounding lender liability under CERCLA, lenders are far more cautious in making new loans and generally require at least a Phase I site audit before making a commitment. This adds time and cost to the transaction (King 1988). As far as old paper is concerned, lenders have to be very wary about foreclosing on properties with environmental liabilities as the cost of cleanup can often be far more than the property is worth. When a borrower is in bankruptcy the lender must be careful not to become too involved in the operations of the facility (Glass 1987). It is possible to write the loan document so that the borrower indemnifies the lender against environmental liabilities, yet this does not excuse liability under CERCLA (Hammers 1990).

The uncertainty instilled by CERCLA for business and particularly for lenders makes planning difficult and prompts changes in business practices to allow for the uncertainty. This of course costs time and money. The irony is that despite site audits and environmental indemnification clauses, there is still uncertainty about the liabilities imposed by the Act, now and in

the future. A clearer picture of liability would be beneficial. As it stands a great deal of energy is expended guessing as to the extent of liability and attempting to protect against a worst case scenario.

The Battle over Insurance Coverage

The insurance industry, while not directly liable under CERCLA has much at stake in the ongoing battle over who shall pay for toxics cleanup. As PRPs are targeted for the costs of cleanups, they are turning to their insurance carriers to share the burden (Cheek 1988). After initial setbacks in court, insurers are now winning cases and thus being absolved of liability. (Hoskins 1989). The conflict is over Comprehensive General Liability (CGL) policies and the definitions they contain. Since these are standard form policies, the definitions are the same throughout the country and the arguments then come down to differences between jurisdictions as the courts try to sort through the complexities and ambiguities of the policies (Hoskins 1989). While the major corporations and large insurance companies are fighting on equal ground at this point, there is a strong possibility that local courts may find for the smaller PRPs when their cases come to trial, because juries may be sympathetic to the little guy (Cheek 1988). A more progressive approach may be negotiation of cost sharing as opposed to the huge

unproductive transaction costs of extended litigation. It should be noted that because of the uncertainty and tremendous costs involved with toxics cleanup, insurance for environmental damage is virtually unavailable at this time (Barnard 1987, Davis 1990).

Recommendations

While the potential liabilities arising from CERCLA are great, defenses are few. In practical terms, all parties potentially open to CERCLA liability should take the all available steps to protect themselves. For the buyer in a real estate transaction, an environmental site audit is essential. The seller should desire this step as well, even if it brings bad news, because the cost could be higher if the problem is left untended. The lender should also demand a site audit as a condition of the loan, as well as require an environmental inspection easement to allow access to the site for an audit should foreclosure be necessary (Gebhardt 1990).⁴ Lessors and lessees should also perform an audit before concluding a lease agreement so each party will be aware of the initial condition of the property (Hayes 1989). While there is no assurance that an environmental audit affords ironclad protection, it is the only protection available at this time and with the extremely costly risk associated with CERCLA liability, a prudent move.

CONCLUSION

The potential environmental liabilities imposed by CERCLA are tremendous. CERCLA broadly defines Potentially Responsible Parties while allowing narrow defenses to liability (Summers 1990). The courts have greatly expanded liability with very little legislative history to guide them (Glass 1987). The effect is one of great uncertainty for the business community. The Act was designed to clean up the hazardous waste problem with the polluters paying the bill. In reality very few sites have been cleaned up and the government record on collecting from polluters is dismal (Smith 1989).

The EPA policy of hunting for deep pockets, particularly in the lending industry, is actually having the opposite to its intended effect of promoting clean-ups (Corash 1990). Lenders avoid foreclosure to avoid liability, and hazardous waste sites go unreported. The situation for lenders is very much in doubt and as such lending practices have changed to reflect the uncertainty. Capital is not available to those at risk of CERCLA liability, and innocent parties are made to pay for problems they did not cause (Corash 1990). This is a conflict inherent in CERCLA between the goal of cleaning up hazardous waste and the rights of innocent property owners (Cornell 1989). While the purpose

of CERCLA is to clean up sites, the major result at this time is costly litigation (Lyons 1987).

CERCLA is onerous in comparison with the European approach. The European Community recently enacted legislation to deal with its hazardous waste problems that is cooperative and includes cost-benefit analysis. The cost of this program will be lower than the adversarial CERCLA in the U.S. This does not bode well for competitiveness of the U.S. compared to the EC (Freeman 1990) .

The uncertainty spawned by CERCLA makes business planning difficult and will continue to drive businesses that are potentially liable under U.S. environmental laws offshore. Some would favor this. The costs of compliance may represent an excuse to export jobs and capital with the standard explanation about an unfriendly business climate at home. It may be better to keep business here and promote cleaner and more efficient processes rather than polluting the Third World even more. If the spectre of Superfund liability looms over companies and capital is unavailable, this will not be possible.

Congress has the power to change the hazardous waste statutes. CERCLA is due for reauthorization this year. The last reauthorization was two years late and the expectation is that it may be 1992 before action is

finalised this time (Berz 1991). There are two amendments pending to provide relief to innocent parties to real estate transactions, one dealing with the innocent landowner defense and the other with lender liability. Rep. Curt Weldon's H.R. 2787 defines environmental due diligence for the purpose of qualifying for the innocent landowner defense. The steps of a Phase I audit are specifically enumerated (Hayes 1990).⁵ This bill would give far more certainty to the innocent landowner defense, in which there is some doubt at this point. Another amendment being offered is a strengthening of the security interest exemption. H.R. 2085, offered by Rep. John LaFalce, changes the definition of 'owner or operator' by specifically exempting "any designated lending institution which acquires ownership or control of the facility pursuant to the terms of a security interest held by the person in that facility." (H.R. 2085 from Berz 1991). This bill is plagued by ambiguity and fails to delineate between past and present lenders (Berz 1991, Moelis 1990). Despite these possible amendments, it is unlikely Congress will change much of the complex Act.

Cleaning up hazardous waste sites in the United States is now estimated to cost \$500 billion to \$1 trillion and may take up to 50 years (Cheek 1988). This is a long term project that should be carefully planned

and monies expended for cleanup rather than on law-suits. The present law wastes huge amounts of money on lawyers and experts arguing over who should pay (Lyons 1987). The costs must eventually be spread more evenly across society. As unpalatable as taxes may be, no pocket is deep enough to pay this price. This is a national problem, we need a national solution.

NOTES

1. The complete definition of 42 § USCA 9601.35: The term /contractual relationship / for the purpose of section 9607 (b) (3) [107 (b) (3)] of this title/ includes/ but is not limited to/ land contracts/ deeds or other instruments transferring title or possession/ unless the 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 one or more of the circumstances described in clause (i) / (ii) / or (iii) is also established by the defendant by a preponderance of the evidence:

(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.

(ii) The defendant is a government entity which acquired the facility by escheat/ or through any other involuntary transfer or acquisition/ or through the exercise of eminent domain authority by purchase or condemnation.

(iii) The defendant acquired the facility by inheritance or bequest.

In addition to the foregoing/ the defendant must establish that he has satisfied the requirements of section 9607 (b) (3) (a) and (b) of this title.

(B) To establish that the defendant had no reason to know/ as provided in clause (i) of subparagraph (A) of this paragraph/ the defendant must have undertaken/ at the time of acquisition/ all appropriate inquiry into the previous ownership and uses of the property consistent with good commercial or customary practice in an effort to minimize liability. For purposes of the preceding sentence the court shall take into account any specialized knowledge or experience on the part of the defendant/ the relationship of the purchase price to the value of the property if uncontaminated/ commonly known or reasonably ascertainable information about the property/ the obviousness of the presence or likely presence of contamination at the property/ and the ability to detect such contamination by appropriate inspection.

(C) Nothing in this paragraph or in section 9607(b) (3) of this title shall diminish the liability of any previous owner or operator of such facility who would otherwise be liable under this chapter. Notwithstanding this paragraph/ if 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 under section 9607(a) (1) of this title and no defense under section 9607(b) (3) of this title shall be available to such defendant." (West Publishing 1989) .

2. De minimus settlements under section 42 § USCA 9622(g) (1) (B) may be granted if "[t]he Potentially Responsible Party-

(i) is the owner of the real property on or in which the facility is located;

(ii) did not conduct or permit the generation, transportation, storage, treatment, or disposal of any hazardous substance at the facility; and (iii) did not contribute to the release or threat of a hazardous substance at the facility through any action or omission. This subparagraph (B) does not apply if the potentially responsible party purchased the real property with actual or constructive knowledge that the property was used for the generation, transportation, storage, or disposal of any hazardous substance." (West Publishing 1989).

3. Environmental due diligence involves a site investigation in the form of a Phase I environmental site audit. While not codified at this time, a site audit generally involves a check of previous uses of the site and a basic physical inspection of the property. See Moskowitz, 1989 and Nanney, 1990 for further details.

4. An environmental inspection easement allows the lender to inspect the facility prior to foreclosure. Without this document, the lender has no legal right to inspection; in practical terms, during a hostile foreclosure action this could preclude an environmental audit. Without the audit there is the danger of environmental liability for the lender. See Gebhardt, 1990 for more detail.

5. Rep. Weldon's bill would codify environmental due diligence for the purpose of the innocent landowner defense. Under H.R. 2787, a Phase I audit would include the following elements: title history, previous uses, adjacent property uses, aerial photographs, interviews with neighboring property owners and employees of the facility, government agency listings, site inspection and recommendations as to the necessity of a Phase II audit. If further study is indicated and the PRP ignores this, the PRP is disqualified from using

the defense. For complete text of the bill, see Nanney, 1990.

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