

A PRIMER ON SUPERFUND

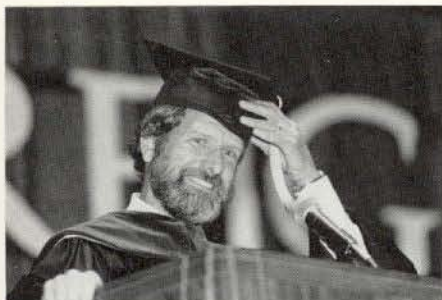
by Professor Eric Pearson

This article is an adaptation and update of a presentation given last year at a Creighton University School of Law Continuing Legal Education program entitled "Dealing with the Resolution Trust Corporation and Related Current Real Estate Issues."

By this late date, only the cloistered have not heard about "Superfund." People know that Superfund is a federal something or other having to do with hazardous waste clean-up. They know that there are lots of hazardous waste dumps around the country,

little and big "Love Canals," and that Superfund is a cache of money collecting dust while the government moves at a perceived only-slightly-faster-than-geologic pace toward actually solving the problem.

But many people who know of Superfund are unclear about its particulars. If



Professor Pearson was voted by the Class of 1991 as "Professor of the Year."

you are one of these persons, and if you would like to learn a bit more about this lurking beast, read on. What I will attempt to do in these next few pages is to give some outline of the liability structure of Superfund, and in the process raise some red flags that might be helpful to real estate buyers and others involved in real estate transactions.

Superfund, as you know, is a federal statute. Formally known as the Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA), it is the latest in a line of pollution control statutes the earliest of which are the famous (infamous?) and oft-amended Clean Air Act of 1970 and Clean Water Act of 1972. These post-Earth Day measures, as their names indicate, addressed severe air and water pollution, and each adopted the conventional approach. Each established a system of standards and penalties applicable to the polluters themselves. Polluters would have to clean up their acts or pay the consequences.

Shortly after enactment of these "flagship" federal statutes, the nation became uncomfortably aware of a troubling additional reality: pollution was not confined to the more readily observable "media" of air and water. Land, also, was serving as a final resting place for contamination, and, in fact, was doing so more often now than the air and water media were off limits. Congress, clearly on a roll, responded with another statutory program, the Resource Conservation and Recovery Act of 1976 (RCRA). This measure aimed to do with land what the Clean Air and Clean Water Acts had done in their respective spheres of operation: it established standards and penalties to deter the land polluters.

THE ARRIVAL OF CERCLA

With RCRA in place, the federal government had accommodated the entire spectrum: it had moved to stop pollution of air, water, and land. So why CERCLA? Simply put, the government kept learning. It learned that scores of hazardous waste dumps already dotted the countryside. Some of these dumps were of recent vintage, but many were old and long-abandoned. These dumps, the U.S. Environmental Protection Agency (EPA) learned, were often filled with indescribable combinations of highly toxic waste chemicals, which would leach, mix, and mingle with the surrounding environment, creating health hazards as they went along.

The dumps presented new and intriguing regulatory problems for the EPA. First, it became clear that stopping land pollution, as RCRA was designed to do, would not remove the problem of existing hazardous waste dumps. RCRA, rather, would arrest future worsening of the problem, but could not tackle the problem of pre-RCRA dumping. And land pollution was here to stay. The air and water media might be able to clean themselves after the polluters stopped polluting, but the land would not. The land needed someone to do its cleaning for it. But who? The EPA could not find the persons who long ago polluted many of these sites; those dumpers were long gone. Something had to be done. And it shall be called "Superfund."

CERCLA was enacted in 1980, and was amended five years later. It addresses the problem of toxic land pollution in two ways. First, as its nickname instructs, CERCLA establishes a large fund of monies designated for hazardous waste clean-up. The fund originally received an allocation of \$1.6 billion for use through 1985; in 1986, Congress allocated another \$8.6 billion to it for use through 1991. (These are big numbers, but the fund no longer seems so "super" when compared with the savings and loan industry bailout operation).

The EPA can use this fund in appropriate cases, but it would rather not. It prefers instead to find persons, i.e. individuals, i.e. non-governmental entities, to

do the clean-up at their expense, thus sparing the public coffers. CERCLA, in its second so-called "remedial" approach, gives the EPA this opportunity by assessing liability on persons. It is this statutorily created personal liability that distinguishes CERCLA from its predecessor pollution control statutes. CERCLA assesses liability not upon polluters, but upon persons who may have had absolutely no involvement in, as the statute terms it, "the release of a reportable quantity of a hazardous substance." In other words, it finds people who are not polluters liable for pollution. (In a real sense, therefore, CERCLA is not a pollution control statute at all; it is, rather, a pollution repair statute).

LIABILITY UNDER CERCLA In General

Superfund imposes liability for hazardous waste clean-up upon four groups of persons ("persons" includes organizations and governmental entities):

(A) present owners and operators of a Superfund site;

(B) prior owners and operators of a Superfund site, who owned or operated the site when the pollution activity occurred;

(C) any persons who arranged for treatment, transport, or disposal of hazardous substances at the site (usually, so-called "generators" of hazardous waste); and

(D) any persons who accepted hazardous substances for transport or disposal at the site (usually, so-called "transporters" of hazardous waste). CERCLA Section 107(a).

Liability categories (C) and (D), which cast liability on generators and transporters, strike many people as appropriate, since generators and transporters have some traceable past involvement with the polluting materials themselves, and presumably made some profit from that involvement. Asking generators and transporters to clean up, therefore, is not so controversial. Categories (A) and (B), though, which cast liability on persons who own or operate the land, either currently or when the dumping occurred, have raised considerably more eyebrows.



In many instances, these persons are free of fault by any standard measure, yet may still be required to fork up immense hazardous waste "response costs." These persons are liable largely due to the Doctrine of Bad Luck, and in the unhappy case can be made to bear the entire expense, even when others share liability. As one EPA official has termed it, CERCLA liability is "strict, joint, several, and perpetual."

It is this prohibitive possibility, the out-of-the-blue potential imposition of a crippling legal responsibility to finance a soil excavation, treatment, and quarantining operation, that gives rise to the seminal question about Categories (A) and (B). Just who is an "owner" or "operator" anyway? One would think that Congress in its wisdom would have given some thought to these springboard questions. But one would be wrong. CERCLA describes "owner" essentially as "one who owns" and "operator" as "one who operates." Congress seems to have a limited vocabulary.

Owners

So, those of us worried about debilitating liability are left to speculate as to the meanings of these foundational terms. As any Property law student can tell you, the meanings of these terms are not self-evident. Consider the term "owner." Certainly, one who owns fee simple absolute title would qualify as an owner, but what of the life tenant, the trust beneficiary, the lessee of a term of years, the easement holder? Are these interest holders also owners? We really do not know; case law has not drawn these lines for us. We can safely speculate, of course, that the more "property" one holds in land, the greater the likelihood of finding CERCLA ownership. But we sure would like to know more.

What of a successor corporation? A successor corporation is one which takes over another corporation, typically by merger, and extinguishes the former in the process. As the new owner, does a successor corporation take on the CERCLA liabilities of the entity it extinguishes? Or does CERCLA liability cease when the originally liable entity ceases? Here, the courts have given us answers.

The United States Court of Appeals

for the Third Circuit has held that successor corporations may be liable for the CERCLA liabilities of the entities they take over. *Smith Land & Improvement Corp. v. Celotex*, 851 F.2d 86 (3d Cir. 1988). That court reasoned that the common law which governs successor corporation liability should apply in this context, also. The court noted further that

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liability should not be easily avoided by the gambit of arranging a merger or consolidation. Thus, the Third Circuit applied the common law which allows for liability of successor corporations generally if:

- (1) the purchasing corporation agrees expressly or impliedly to assume liability;
- (2) the transaction is equal to a de facto consolidation or merger;
- (3) the purchasing corporation is a continuation of the selling corporation; or
- (4) the transaction was fraudulently entered into.

The Sixth and Ninth Circuits have ruled similarly. See *Anspec Co. v. Johnson Controls, Inc.*, 922 F.2d 1240 (6th Cir. 1991); *Louisiana-Pacific Corp. v. Asarco*, 909 F.2d 1260 (9th Cir. 1990). At least four district courts (in Massachusetts, North Carolina, Kentucky, and Michigan) also have made similar rulings.

It is uncertain whether a corporation

acting in a custodial capacity — acting as a receiver or conservator of the assets of an entity which itself does not go out of existence — assumes CERCLA liability.

What of a lender? Is a lender an owner because it has a mortgage or other security interest in contaminated land? With uncharacteristic attention to detail, CECLA answers this question in the negative. CERCLA expressly states that a "person" who "holds indicia of ownership primarily to protect his security interest" shall not be considered to be an owner. But if a lender finds it necessary to foreclose on a mortgage and thereby takes title to the contaminated land, it then becomes an owner and assumes clean-up liability. For obvious reasons, lenders often elect not to foreclose, in effect to write off a bad debt, rather than assume CERCLA liability.

Operators

The courts have shed some light on the meaning of "operator" in CERCLA. One court said the term as used in CERCLA should be given its ordinary meaning, and should not be read in an unusual or highly technical way. Another court commented that one must participate in "direct management" of the site and have undertaken some "hands-on" activity to qualify as an operator. Another court stipulated that "active involvement" in day-to-day activities was necessary for operator status. Corporations can be operators, and their majority shareholders can be operators also. Of course, individuals can take on this legal status.

Still, as with "owner," the precise meaning of "operator" is not entirely clear. One obvious proof of these definitional ambiguities can be found in the recent brouhaha about lending institutions. We have seen that lenders can be owners for purposes of CERCLA. Lenders can be operators, too. If a lender undertakes the day-to-day operation of a site, it becomes an operator and becomes liable. Moreover, if a lender does less than that, and only "participates in the management of a [site]" the lender will be liable as an operator. CERCLA, Section 101(20)(A). The question becomes, how much participation is too much?

On that latter question, until recently



the prevailing notion was that lenders can participate in *financial* management of a site, and not be liable under CERCLA, but had better stay away from any involvement with day-to-day management decisions. See *United States v. Mirabile*, 23 ERC 1511 (D.C. Pa. 1985). But that understanding is gone since May of 1990, when the first federal appeals court to consider lender liability under CERCLA ruled that liability attaches if a secured creditor's "involvement with a management of [a] facility is sufficiently broad to support the inference that it could affect hazardous waste disposal decisions if it so chose . . ." By this standard, a lender is liable even if it in no way participates in the day-to-day management of a facility or site, so long as it has the power to do so! The liability arises if the lender "participat[es] in the financial management of a facility to a degree indicating a capacity to influence the corporation's treatment of hazardous waste." See *U.S. v. Fleet Factors Corp.*, 901 F.2d 1550 (11th Cir. 1990).

One more recent federal court decision has cast some doubt on this controversial reading. The Ninth Circuit, while taking care to distinguish *Fleet Factors*, said nonetheless that "participation in management" cannot have occurred when a lender has not exercised any managerial powers. *In re Bergsoe Metal Corp.*, 910 F.2d 668 (9th Cir. 1990).

DEFENSES TO LIABILITY

If you find yourself liable under CERCLA, does that mean you automatically lose? The short answer is no. CERCLA provides several statutory defenses. One can avoid liability otherwise imposed by CERCLA by showing that the pollution-causing conduct was:

- an act of war (not much case law to tell us what this means);
- an act of God (your every-spring flood, occasional severe summer storm, or below-zero December is not an "act of God");
- the act of a third party.

Avoiding liability by demonstrating that the pollution-causing activity was accomplished by a third party is difficult. Such a demonstration can remove liability, but note the following: (a) if the third

party which caused the pollution is your agent or employee, you remain liable; (b) if the third party which caused the pollution is acting by virtue of a contract with you, you remain liable. And CERCLA finds a contractual relationship where none other has ventured. An arrangement by which an independent contractor comes on to your land and then causes the pollution obviously qualifies as a "contractual relationship" between that person

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and the landowner, thus stripping away the defense. If the third party has possession by virtue of a land contract, a "contractual relationship" exists so as to strip away the defense. If the third party has title or possession by virtue of a deed or other document (for example, a lease, trust document, and so on), a "contractual relationship" exists so as to strip away the defense.

When will a contractual relationship be deemed not to exist, so that the third party defense becomes available to the landowner? The answer is when one is an "innocent landowner."

When is a landowner innocent? One time is when there is absolutely no relationship whatsoever between the landowner and the third party polluter. Another time is when a landowner took the land after all of the pollution-causing conduct took place, and at the time of acquisition, did not know nor should have

known of any problem of this sort. (There are also two other ways to be an innocent landowner, of less interest to us. They are if the landowner is a governmental entity taking by escheat, eminent domain, or an involuntary transfer or acquisition of title interests; or if the landowner took by inheritance or bequest).

Note, however, that a landowner cannot blissfully buy property and be protected by his or her ignorance of past pollution-causing activity. Under CERCLA, the landowner "knows or should have known" of the pollution problem (so as not to be an innocent landowner) if he or she does not inquire enough or appropriately about the land prior to acquisition. And in deciding whether an owner did inquire enough or appropriately, courts will consider whether the owner is knowledgeable or experienced about these things (which each of you is now, having read this far, sorry); whether the purchase price was suspiciously low; whether the information was "reasonably ascertainable" or obvious; and whether the pollution problem could have been discovered by an inspection.

Regardless of the identity of the third party, though, if the liable person failed to exercise due care or failed to take precautions against foreseeable third party actions or omissions and the consequences that could foreseeably result from such acts or omissions, she or he is liable.

Lastly, and independent of the above information, if a landowner transfers contaminated property to another, and thereby would no longer be liable under the categories of CERCLA, still liability remains if the landowner (a) learned of the problem while in ownership or operation of the property, and (b) transferred the property without disclosing the problem to the purchaser. In such a case, no third party defenses are available.

CONCLUSION

All of us involved in any way in real estate need to know of CERCLA. The liabilities it imposes are potentially enormous. Even though a liable person can force others who are liable to join in and ante up, the most prudent fiscal course is to avoid liability entirely.