

# SCHNAPF ENVIRONMENTAL REPORT

A Newsletter Covering Recent Environmental Developments and Caselaw

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## DUE DILIGENCE/ AUDITING/ DISCLOSURE/ ENFORCEMENT

### *Accounting Scandals Impacting Environmental Due Diligence*

In the wake of the accounting irregularities that have shaken Wall Street, some conduit lenders are becoming increasingly concerned about the quality of the Phase I Environmental Site Assessments ("ESAs") being used for securitized loans. ESAs function like stock analyst reports in securitizations since conduit lenders disclose the results of the ESAs to rating agencies and buyers of their commercial mortgage-backed securities ("CMBS"). With investors and regulators now scrutinizing financial reports, some lenders are concerned that the "commodity-style" ESAs commonly used in CMBS transactions might not be sufficiently examining the environmental conditions of properties that are serving as collateral for the deals.

As a result, some lenders are starting to direct their business away from consultants with reputations for producing "commodity-style" Phase I ESAs and towards full-service environmental consulting firms that perform more thorough site assessments. Other lenders are asking their environmental lawyers to thoroughly review commodity-style Phase I reports or asking consultants to beef-up their reports and fill in information gaps identified by the lenders' environmental counsel.

**Commentary:** With the public and politicians demanding that regulators prosecute professionals who are perceived to have participated in the preparation of misleading or fraudulent financial reports, attorneys and consultants need to be careful about how they edit language in the ESAs. Attorneys need to be careful not to change factual observations made by consultants in Phase I reports. Similarly, consultants should not be so eager to delete or alter factual observations, conclusions or recommendations to please or accommodate their lending clients.

### *ASTM Issues ESA Standard for Rural Property*

The ASTM E1527-00 Standard for Phase I ESAs (the "E1527-00") is designed to identify recognized environment conditions ("RECs") at industrial, commercial or residential properties. This standard is not particularly suitable for large tracts of undeveloped land that may have isolated RECs. However, as development continues to push out into rural areas, consultants are increasingly being asked to assess undeveloped property or properties that have been developed for only a few years.

As a result, ASTM has proposed a new Phase I ESA for Forestland and Rural Property that is intended to satisfy the CERCLA innocent purchaser defense. It is anticipated that the new standard will be used for rural real estate development, transactions involving farmland, land used for cell towers, corridor studies for highways and large holdings of natural resource organizations.

The proposed standard is modeled after the E1527-00 but has some important distinctions. One of the more important differences is the record review requirements. In addition to the records normally reviewed, the proposed standard would include records pertaining to threatened and endangered species and documentation requiring the use of best management practices. Additional local sources of information will include the Department of Natural Resources and Division of Forestry.

The same standard historical sources should be reviewed with the exception of fire insurance maps since undeveloped areas larger than 120 acres were historically not mapped. Local officials that should be interviewed include property managers, farm managers or ranch managers. Environmental professionals are also required to try to interview occupants of

the large tracts such as those involved with hunting clubs, agricultural and silviculture tenants.

One of the problems with large undeveloped tracts of land is that isolated commercial operations could have operated in the past such as mining operations or waste disposal but may not be easily observable. As a result, in addition to the site reconnaissance methods used for the E1527-00, the proposed standard also suggests considering statistical plot systems, a aerial flyover or other approaches used for large tracts of land. To identify potential problematic areas, the proposed standard suggests that environmental professionals look for caves, ditches, and streams that may have been associated with past disposal or waste generation practices.

The proposed practice contains many of the same non-scope items that may be included by the client in the scope of the ESA. Relevant non-scope items for these kinds of properties include conditions that could affect water quality, threatened or endangered species, SMZs and Best Management Practice areas.

**Commentary:** The client will be responsible for determining whether to use the Phase I ESA rural property standard or the E1527-00. If commercial real estate activity is identified during the rural ESA, it would be advisable to perform the E1527-00 for that particular portion of the parcel.

### ***Purchasers Need to Carefully Review Closure Cost Estimates***

The federal Resource Conservation and Recovery Act ("RCRA") requires facilities that treat, store or dispose hazardous wastes ("TSDF") to demonstrate that they have the financial resources to cover their closure and post-closure costs as well as to compensate third parties for bodily injury or property damage. The closure, post-closure and liability financial resources are known as financial assurance. The TSDF must prepare written closure and post-closure plans that estimate the closure and post-closure costs. The amount of third party liability coverage is mandated by RCRA. The sudden accidental coverage is set at \$1 million per occurrence and annual aggregate of \$2 million per facility while the non-sudden accidental coverage is \$3 million per occurrence and \$6 million in the aggregate per facility. The financial

assurance can be in the form of a trust fund, surety bond (payment or performance bond), irrevocable standby letter of credit, financial test, corporate guarantee or an insurance policy. When the business or facility has used an insurance policy for the financial assurance, purchasers will review the rating of the insurer.

During due diligence, purchasers often assume that the financial assurances established by a business or facility are sufficient to cover the estimated closure or post-closure costs if EPA or a delegated state agency has approved the closure plan or financial assurances. Instead, they usually simply evaluate if the financial assurances remain in full force and effect.

However, closure or post-closure cost estimates may not reflect the actual remediation costs for a facility. For example, a facility is only required to estimate closure costs for RCRA-regulated units known as hazardous waste management units ("HWMUs") and not solid waste management units ("SWMUs"). During post-closure, though, a facility will usually be required to investigate and remediate SWMUs that have impacted the environment. In addition, the closure estimates for HWMUs such as a landfill are only required to include groundwater monitoring and not groundwater remediation.

Further complicating the situation is that the facility may become subject to a corrective action order that may accelerate cleanup costs that a business did not anticipate to spend for another decade or two as well as costs that were not included in the original estimates such as groundwater remediation or cleanup of SWMUs.

In addition, there are different methods that may be used to calculate the amount of closure costs. For example, the owner of a landfill may apply a portion of the tipping fees received towards its closure obligations or may develop closure costs by multiplying the disposal rate by the remaining disposal capacity of the landfill. As a result, it is important for purchasers to review the assumptions and calculations used to develop the closure and post-closure costs.

**Commentary:** When a TSDF or HWMU ceases receiving wastes, the owner/operator must either remove the wastes which is known as "clean closure" or take steps to

minimize the possibility that hazardous waste constituents will escape into the environment from the HWMU or TSDF. The owner or operator of a TSDF or a HWMU must notify EPA or the delegated state agency at least 60 days before the owner/operator expects to begin closure of a surface impoundment, waste pile or land treatment unit or 45 days prior to the expected closure date of a storage tank, container or incinerator. The date when an owner "expects to begin closure" is either 30 days after the HWMU receives its last volume of hazardous wastes or if there is a reasonable possibility that the HWMU will receive additional hazardous wastes, no later than one year after the date the HWMU received its most recent volume of waste.

#### ***Phase I ESAs and Lead-Based Paint***

The E1527-00 is intended to satisfy the "appropriate inquiry" that is necessary to establish the Innocent Purchasers Defense of the Comprehensive Environmental Response, Compensation and Liability Act ("CERCLA"). The E1527-00 is designed to identify RECs which are defined as the presence or likely presence of hazardous substances or petroleum that indicate there is an existing release, past release or a material threat of a release of hazardous substances or petroleum.

Because the E1527-00 is focused on the CERCLA Innocent Purchaser defense, other common substances that can result in liability at commercial or residential real estate such as asbestos, lead-based paint ("LBP"), lead in drinking water ("LIW"), radon and wetlands are outside the scope of the standard. However, many banks have added these so-called non-scope items to their E1527-00 requirements.

For LBP, many lenders require a consultant to collect a certain number of samples when performing a Phase I ESA at residential property constructed prior to 1978. If LBP is detected, the borrower will usually be required to implement a LBP operation and maintenance ("O & M") plan. However, lenders do not usually require consultants to review tenant files to determine if the borrower has complied with the LBP disclosure rules.

**Commentary:** prior issues, we have discussed EPA's LBP enforcement initiative where the agency has been conducting random inspections of residential properties

to determine if the landlords have been providing tenants with the required LBP notices. These inspections have resulted in significant fines and occasionally criminal penalties. In addition, properties that are in violation of the LBP disclosure requirements are placed on list of sites under the Toxic Substances Control Act ("TSCA"). To determine the potential liability that a borrower may have for LBP violations, a lender should consider requiring consultants to randomly review tenant files when performing Phase I ESAs on housing built prior to 1978.

#### ***EPA Continues Enforcement Initiative Against Universities***

EPA penalized Pratt \$301,000 for seven violations of RCRA. The violations involved improperly handling old or obsolete chemicals, spent solvents and paint, used fluorescent light bulbs, computer monitors and other wastes generated by or used in Pratt's art studios and workshops. Within 30 days of the compliance order, Pratt is required to comply with, or provide a schedule to comply with all applicable federal and state hazardous waste regulations and to cease burning solvents

Manhattan College in the Bronx, New York was fined \$111,199 for three RCRA violations. EPA alleged that Manhattan College failed to determine if certain solid waste constituted hazardous waste, improperly stored hazardous wastes and failed to respond to two EPA information requests. The violations involved mercury, arsenic, spent solvents and paint, used fluorescent light bulbs, used computer monitors and other wastes generated by or used in the Manhattan College print shop, labs and maintenance facilities at its two Bronx facilities. Within 30 days of the compliance order, Manhattan College is required to submit a written notice of compliance. If Manhattan College is not in compliance, it must state the reasons for the noncompliance and provide a schedule for achieving prompt compliance.

**Commentary:** 48 colleges and universities in EPA Region 2 have participated in EPA's Colleges and Universities Initiative and have received 100% waiver of gravity-based penalties. 14 cases are still under review and the remaining others have been partially approved. In addition, we discussed in our prior issue that Rutgers University and the

State University of New York agreed to undertake a long-term auditing program in exchange for reduced penalties under EPA's Audit Policy.

### ***Criminal Action Brought Against Oil Supplier For Failing To Disclose UST Leak***

While examining the elements of the new CERCLA prospective purchaser defense in our last issue, we discussed the complexity of the requirement to comply with all release reporting requirements. A recent New York case involving a leak from an underground storage tank illustrates the confusion that can surround reporting requirements.

In *People v. Meenan* (No. 11919/01, N.Y. Dist.Ct. Nassau Co.), the defendant oil supplier was called to a residence because of an oil spill where he determined the spill was caused by a leak in the fill line of the fuel oil tank. The leak occurred inside the premises and seeped underneath the cement basement floor. After the defendant notified the county health department, a criminal proceeding was initiated against him for failing to report the spill to the county fire marshal. The defendant sought to dismiss the action, arguing that it was not required to report the spill to the fire marshal but even it was, it had satisfied its obligation by disclosing the spill to the health department.

In the hearing, the county indicated that Article III of the Nassau County Fire Prevention Ordinance (NCFPO) clearly provided that "any person with knowledge of a spill, leak or discharge" of a flammable or combustible liquid was required to report the incident within two hours of discover. In addition, this section also provided that the results of any inventory test or inspection that shows a facility was leaking also had to be reported within two hours. The ordinance went on to say that this reporting obligation did not relieve the "spiller" of any obligation to report the spill or discharge to the state Department of Environmental Conservation

("NYDEC").

The defendant argued that the NYDEC had delegated the enforcement of the UST program to Nassau County and that the county had split the jurisdiction of the program between the health department and the fire marshal, with the health department responsible for tanks that are connected to residential or commercial building heating systems while the fire marshal was responsible for all other tanks. The defendant pointed to Article XI of the NCFPO that provided that an owner or other person in possession or control of any storage or transfer facility or "any person with knowledge" shall report any possible unauthorized spill, leak or recognizable loss of toxic or hazardous materials by the fastest means possible within two hours to the health department. This provision also said that a report to the health department would not be deemed to constitute compliance with the reporting requirements of any other federal, state or local law. The defendant also indicated that there was confusion over the reporting requirements and that in the past oil companies reported to all three agencies, just the DEC or simply the fire marshal.

The court held there was no specific provision excluding reporting to the fire marshal or any evidence that the legislature intended to exempt storage tanks connected to heating systems from the fire marshal reporting obligations. The court said the language of the NCFPO clearly showed that the legislature contemplated that there might be dual reporting requirements to different agencies. The court went on to suggest that the defendant and the heating oil industry contact the legislature to have a specific exclusion placed in the statute to avoid any confusion.

## **ENVIRONMENTAL INSURANCE**

### ***"Lesser of" Secured Creditor Policies Playing Larger Role in Transactions***

In past issues, we have discussed how loan balance secured creditor policies can be used to facilitate transactions. However, these policies have become very

expensive during the past nine months and the underwriting has tightened considerably. Exacerbating the pricing trend is that "B" buyers in CMBS transactions are requiring stand alone policies for loans over \$3.5 million that cover 125% of the loan balance.

In addition, a stand alone policy will be required for each secured note for each property. Thus, a policy covering individual cross-collateralized loans or individual properties within a portfolio of mortgages that are cross collateralized and secured by one mortgage loan will not be acceptable. (see our March issue for more details about changes in the secured creditor policy market).

As a result, secured creditor policies known as "lessor of" policies are now playing a larger role in transactions. These policies will pay either the remaining loan balance or the cleanup costs, whichever is less. Since the premium is not based on the entire loan balance, these policies can be much cheaper than the loan balance policies and adequately protects lenders against loss in collateral value. Another good feature of the lesser of policies is that they may be able to be purchased with any deductible which is also known as the self-insured retention ("SRI").

#### ***Using the "Known Conditions" Coverage in Environmental Insurance Products***

The old Comprehensive General Liability ("CGL") policies that were commonly used between 1985-1995 usually had an exclusion for pre-existing pollution conditions that the insured knew or should have known could give rise to a claim. These policies were obviously not useful for brownfield sites since the very reason sites are considered brownfields is the existence or suspicion of contamination.

In response to the growing popularity of brownfield programs, insurers have introduced a number of the new environmental insurance products such as the pollution legal liability or cleanup cost cap policies that allow purchasers of

contaminated property to obtain coverage for pre-existing known environmental conditions that are disclosed to the insurer during the application process. This coverage can be used for costs that are in excess of a SRI. It is also useful as a backstop for reopeners that are used in most "no further action" letters issued by state agencies. Thus, these policies could provide coverage if contamination from a particular hazardous substance is more widespread than previously believed, for off-site damages caused from known contamination that was thought to be confined to the site and for regulatory changes that may require cleanup of contaminants that currently do not have to be remediated.

To include this coverage, the insurance underwriter will need to review information about the site. Obviously, the more completely that a site has been characterized, the easier it will be for the underwriter to assess the conditions of the site. However, complete delineation of a site may not be necessary. Often times, underwriters can use their experience with the particular contaminants involved at a site or the regulators of a state to evaluate the risk.

Sometimes the coverage is included within the policy but other times the policy will exclude known conditions but then add the coverage by endorsement. To avoid disputes with insurers in the future about what conditions were disclosed, it is advisable to have the a definition of disclosed known pollution conditions that refers to a schedule where all documents provided to the insurer are listed (See our March 2002 issue for more detail about disclosure schedules for insurance policies).

## **AIR POLLUTION DEVELOPMENTS**

### ***EPA Proposes NSR Reforms***

EPA recently issued the results of its 90-day review of the New Source Review ("NSR") program. The study recommended changes to streamline the NSR process and provide more certainty to regulated facilities. Specific changes will be in proposed in draft regulations.

One proposed change is to develop plantwide applicability limits ("PAL") which

would be similar to the EPA "bubble" rule. Under the proposed PAL, facilities will establish plantwide emission caps and be able to make changes to sources without undergoing NSR if they stay within their PAL. The facility would obtain a PAL based on its actual emissions baseline. The PAL would be effective for ten years at which point the PAL would be reevaluated.

Another recommendation is to

create a Clean Unit Exclusion. A source would be considered clean if it previously underwent a permit review process that resulted in the installation of Best Available Control Technology ("BACT"), Lowest Achievable Emission Rate ("LAER") or comparable state minor source BACT. A source that installed Maximum Achievable Control Technology ("MACT"), Reasonably Available Control Technology ("RACT") or undertook pollution prevention measures that required capital expenditures might also qualify for the exemption if the control measures are determined to be comparable to BACT or LAER at the time the controls were installed. The exemption would apply for 10-15 years from the time the control technology was installed or the project implemented. A clean unit would only trigger NSR if a change would result in increased emissions.

The report also proposed to change the Prevention of Significant Deterioration ("PSD") and Non-Attainment permit programs to provide exclude projects that add, replace or change existing sources from NSR and that result in a net overall reduction of air pollution such as changing to cleaner burning fuel. The changes cannot result in an emissions increase that will cause a violation of a National Ambient Air Quality Standard ("NAAQS"), PSD increment or result in an adverse impact to a Class I area. Changes that meet these requirements will not be considered a "major modification" subject to NSR. EPA intends to publish a list of environmental beneficial technologies that will be presumptively eligible for the exclusion. Technologies not on the list will have to be evaluated to determine if they qualify for the exemption.

In connection with these emissions changes, EPA proposes to change the way it calculates emissions increases for all industrial sectors. Currently, facilities must compare pre-modification emissions with *projected* post-modification emissions when operating at maximum capacity. Under the proposed reform, owners and operators of facilities would determine emissions increases for physical changes or changes in operation by comparing representative pre-change actual emissions with projected post-change *actual* emissions. For non-electric utility steam generating units, the actual emissions baseline will be the highest

consecutive 24-month period within the immediately preceding ten years taking into account current emissions factors such as emissions limitations and permanent shutdowns. When calculating post-change actual emissions, EPA will allow facilities to exclude emissions increases that could have been accommodated before the change within the representative baseline period and that are attributable to an increase in projected utilization capacity at the unit that is unrelated to the particular change.

One of the most controversial aspects of the NSR program has been the definition of routine repairs and maintenance activities ("RMR&R"). A change that qualifies as a RMR&R is exempt from NSR review but there has been considerable uncertainty on what exactly is a "routine" activity. To provide more certainty, EPA will establish a cost-based threshold. Projects whose aggregate costs are below the threshold will be automatically deemed to be RMR&R. Projects that exceed the safe harbor cost threshold could be eligible for RMR&R treatment on an individual basis according to guidelines EPA will establish. Costs for installing and maintaining pollution control technology will not be included when calculating the safe harbor threshold. The report also proposes to exclude from the definition RMR&R replacement of existing equipment with equipment that serves the same function and does not alter the basic design parameters of the unit. The study also proposes development of guidelines for activities undertaken to facilitate, restore or improve efficiency, reliability, availability or safety within normal facility operations. EPA may also develop categories of projects in industrial sectors that will be considered RMR&R. For example, in the utility sector, equipment that is maintained, repaired and replaced can be categorized along functional lines such as boiler tube assemblies, air heaters, coal handling equipment, pumps, fans, etc. EPA could identify RMR&R that satisfies the guidelines. EPA would also focus on projects that promote energy efficiency or could result in generator failure that could create safety concerns if delayed. With refineries, the agency may identify RMR&R that are undertaken during "turnarounds".

The report also suggests a rule to clarify how NSR applies when a company

modifies one part of a facility so that throughput increases in other parts of the facility in a process called "debottlenecking". The agency said that emissions from sources upstream or downstream from the unit being changed should be evaluated only when the change will result in emissions from the emissions limits of those upstream or downstream units are exceeded or increased.

When multiple projects are implemented in a short period of time, a complex analysis must be performed to determine if the projects should be treated separately or together (i.e., "aggregated") under NSR. For purposes of NSR review, EPA will propose that a project will be evaluated separately from the other projects at a major stationary source unless the project is dependent on another project to be economically or technically viable or the project is intentionally split from other projects to avoid NSR. EPA said it would generally defer to states to implement the aggregation rule.

**Commentary:** The NSR program was established when the Clean Air Act ("CAA") was enacted in 1970. Instead of regulating existing plants, Congress decided to impose air pollution controls on new facilities. The idea was that air pollution would be reduced as the older facilities were retired and replaced with plants that were complying with the more stringent emission limitations. Power plants generating more than 73 megawatts that were constructed after August 17, 1971 had to comply with new source performance standards ("NSPS"). Existing plants that made "major modifications" by a physical change or change in operations that resulted in emissions increases would have to undergo NSR. However, the NSR permitting process is costly and time-consuming. This regulatory scheme established an incentive to keep older plants in operation and to refrain in making investments in more efficient and cleaner plants.

According to a recent report by the General Accounting Office ("GAO") "Emissions from Older Electricity Generating Units", 57% of the active fossil fuel power plants were operating prior to 1972. 59% of the sulfur dioxide ("SO<sub>2</sub>"), 47% of the nitrogen oxides ("NO<sub>x</sub>") and 42% of the carbon dioxide ("CO<sub>2</sub>") emissions in 2000

were attributable to these older plants. 36% of the older facilities had SO<sub>2</sub> emissions in excess of the NSPS and 73% exceeded the NSPS for NO<sub>x</sub>. For equal amounts of electricity generated, the older facilities emitted twice as much SO<sub>2</sub> as the newer plants and 25% more NO<sub>x</sub>. These excessive emissions are concentrated in the Mid-Atlantic, Midwest and Southeast with older units in those regions accounting for 87% of all SO<sub>2</sub> emissions, 75% of NO<sub>x</sub> and 70% of CO<sub>2</sub>. Older coal-burning units generate 99% of the SO<sub>2</sub>, 88% of the NO<sub>x</sub> and 85% of the CO emitted by the older units. The report indicated that many older units had installed pollution control equipment yet still exceeded NO<sub>x</sub> NSPS.

The GAO report did say that if older units were required to install NSPS by 2000, newer units would have had to increase operations to meet electricity demands. However, the report said it would not be possible to quantify what emissions would have been in 2000 if the older units were retired. Indeed, the report suggested the net decrease of SO<sub>2</sub> emissions might not have been that large since the new units could have purchased SO<sub>2</sub> allowances from the retired units to meet additional electrical demand.

### ***EU and Japan Ratify Kyoto Protocol***

The Kyoto Protocol moved one step closer to reality when Japan and the European Union ratified the treaty. The treaty requires industrialized nations to cut emissions by an average 5% by 2012 from 1990 levels. To become effective, 55 nations producing 55% of the world carbon dioxide emissions must ratify the pact.

Meanwhile, Australia which has signed the agreement in 1997 decided not to ratify it. Australia is the world's largest coal exporter and had the right to increase its emissions by 8% above 1990 levels. Australia was in an unusual position because it is considered a developed nation that is also a massive net exporter of energy. The Australian government said the treaty was flawed because it did not impose reduction targets on developing nations.

### ***California Enacts First Greenhouse Gas ("GHG") Emissions Limits***

As reported in our last issue, California did become the first state in the

nation to regulate GHG emissions from cars and trucks. The new legislation directs the California Air Resources Board ("CARB") to develop regulations to achieve "maximum feasible and cost-effective" reduction of greenhouse gases, including carbon dioxide. The standards would take effect in 2006 and start with the 2009 model year. The bill prohibits CARB from raising vehicle taxes, banning certain types of cars or trucks or reducing current street and highway speed limits.

**Commentary:** Transportation accounts for 61% of GHG emissions in the California

### ***New York Asbestos Enforcement Actions Continue***

During the past year, we have been reporting on the asbestos enforcement initiative in New York that EPA launched following the discovery of widespread non-compliance asbestos regulations in upstate New York. Recently, two managers of an asbestos abatement firm in Latham, New York pleaded guilty to 14 felonies. In *U.S. v. Salvagno* (N.D.N.Y. No. 02-CR-51, 07/02/02), the government alleged that the defendants failed to comply with asbestos work practices thereby releasing asbestos in buildings, obtained falsified laboratory results and destroyed evidence. The firm general manager faces a maximum penalty of 77 years in prison and a fine of \$3.5 million. The field supervisor faces a maximum sentence of 15 years in prison and a \$1 million fine.

Meanwhile, three of the defendants who were previously indicted as part of a larger case involving the illegal removal of asbestos at multiple locations over a 10-year period pleaded guilty. One defendant faces a maximum sentence of up to 25 years in prison and a fine of up to \$1.25 million while the other two defendants face up to 15 years in prison and a fine of up to \$750,000.

### ***EPA Announces Additional Criminal Asbestos Settlement***

Spartan Environmental Remediation Barons Inc. of Sparta, N.J., and three of its employees all pleaded guilty to violating the federal asbestos workpractice rules. Spartan was retained by a general contractor to remove asbestos from seven buildings at the Military Ocean Terminal-Bayonne in Bayonne, N.J. When sentenced, each individual defendant faces a maximum

sentence of up to five years in prison and a fine of up to \$250,000. Spartan faces maximum fines of up to \$500,000 when sentenced.

A doctor and a property management company pleaded guilty illegally removing and disposing asbestos from buildings in Staunton, VA in a variety of locations, including a landfill and dumpsters in and around the city. In *U.S. v. Davold Real Estate Partnership* (W.D. Va., 5:01-CR-30064, 5/28/02), the doctor pleaded guilty to illegally disposing of asbestos-containing material and the partnership pleaded guilty to illegally removing asbestos. The doctor operated buildings owned by the property management company. The defendants hired homeless people and other workers to remove a sbestos insulation from pipes and boilers but did not tell them that they were removing asbestos nor provide them with any training or protective equipment. When sentenced, the doctor faces a maximum penalty of up to five years in prison and a \$250,000 fine while the management company could be fined as much as \$500,000.

Meanwhile, an officer and director of an Alaska asbestos abatement contracting company pleaded guilty to illegal concealment of a felony by failing to report illegal removal of asbestos from the Alaska Pulp Corp. in Sitka, Alaska. The individual was responsible for assuring that all asbestos was properly removed. During the project, the defendant learned that slushy waste containing asbestos abatement waste was allowed to enter a drain system at the facility and flow directly into the local bay but he concealed the violation.

### ***EPA Study Finds that Ethanol Industry Underestimates Air Emissions***

During the past decade, EPA has been targeting certain industrial sectors to determine compliance with the CAA. The next industry that will likely receive scrutiny is ethanol producers because an EPA 17 month study revealed that these facilities have been violating the CAA by emitting dangerous levels of carbon monoxide ("CO"), methanol, formaldehyde, acetic acid and carcinogens.

EPA indicated that the ethanol industry underestimated its emissions, with some plants predicting they would not exceed 100 tons annually. However, EPA

tests found some plants were emitting as much as 1,000 tons a year. EPA estimates it will cost roughly \$1 million for each plant to install the necessary pollution control equipment.

**Commentary:** The ethanol industry currently generates approximately 2.3 billions of gallons of ethanol each year. Ethanol can serve as an oxidizer in gasoline to reduce smog. With a dozen states banning methyl tertiary butyl ether ("MTBE") as gasoline additive, ethanol production is expected to increase. There are currently 61 ethanol facilities spread among 20 states. Most of the facilities are located in the Midwest with Minnesota having the most facilities. However, the four plants in Illinois have the most capacity at 700 million tons per year.

#### ***Study Finds Greater Risks from Radon***

Researchers at the University of Iowa College of Public Health have concluded that the health risk posed by residential radon exposure may have been underestimated by as much as 50%. The results of the study appeared in the May 2002 issue of the Journal of Exposure Analysis and Environmental Epidemiology.

The study examined several exposure models used in previous residential radon studies in North America, Europe and China and compared them to actual measurements within homes. The results indicated that the prior models produced lower risk estimates with the highest discrepancy for risks based solely on basement radon measurements. While radon concentrations tend to be highest in basements, the study said that people typically spend limited time there. As a result, the study said a more accurate risk assessment should involve multiple radon measurements within a home where occupants spend most of their time

#### ***Pharmaceutical Company Fined for CFCs Violations***

EPA recently entered into a settlement with Roche Vitamins to resolve allegations that the company had improperly released chlorofluorocarbons (CFCs) into the atmosphere at its manufacturing plant in Belvedere, New Jersey. An EPA inspection of Roche's service records revealed that Roche had not conducted follow up repairs of one of its large industrial process refrigeration units. The failure to conduct leak repair verifications may have led to a

failure to repair leaks and retrofit or retire the unit. In addition, because some of the service records were missing, there is no way to tell if and how much CFC might have leaked or been released. As part of the settlement, Roche agreed to implement a CFC leak detection and repair program to comply with the CFC regulations. It has also retrofitted the industrial refrigeration unit and has agreed to pay a penalty for the past violations.

#### ***Debate Over Trading Program For Mercury Emissions***

In December 2000, the Clinton Administration decided to regulate mercury as a toxic air pollutant under section 112(n)(1)(A) of the CAA and to develop MACT standards for mercury emissions. The mercury MACT standard may be proposed in 2003 and is supposed to become effective in 2007. Although MACT standards for mercury are not yet completed, the mercury MACT is expected to require at least a 90% reduction in emissions. This would limit mercury emissions in 2008 to 14 tons.

Earlier this year, though, the Bush Administration unveiled its Clear Skies Initiative ("CSI") that would create a national cap and trade program for many pollutants including mercury. CSI would initially cap mercury emissions at 26 tons in 2010 and 15 tons by 2018, a 69% reduction

**Commentary:** There is considerable debate whether a cap-and-trade system should be developed for mercury. The controversy centers on how the two forms of mercury that are emitted by coal-burning plants behave in the environment. Divalent mercury which is also known as reactive gaseous mercury ("RGM") oxidizes in water and settles to the ground fairly close to its emission source. Elemental mercury, on the other hand, is insoluble in water and can be transported for hundreds or thousands of miles before it is deposited on land or water. Once deposited, the chemical form of mercury can be converted into a more toxic form known as methylmercury which bioaccumulates in the food chain. Power plants that burn bituminous coal emit roughly 60% RGM and 40% elemental mercury while mercury emissions from plants burning sub-

bituminous or lignite coal have 95% elemental mercury. Approximately 60% of coal-fired power plants in the United States use bituminous coal.

Those opposed to creating a cap and trade program for mercury say mercury behaves differently in the atmosphere than SO<sub>2</sub> and NO<sub>x</sub> and is not a good candidate

for emissions trading. They claim that elemental mercury is quickly converted to RGM and that a cap and trade program will result in mercury "hot spots" in communities near the power plants.

## WATER POLLUTION/ENDANGERED SPECIES

### ***SWANCC Decision is Not Basis to Overturn Prior Conviction***

In 1996, a jury convicted James Wilson and Interstate General Co. of knowingly discharging fill and dredged materials into wetlands. A federal district court sentenced the Wilson to 21 months imprisonment and a \$1 million fine while imposing a \$3 million penalty on the company. The Court of Appeals reversed and remanded the matter to the district court for further consideration of the wetlands jurisdictional issue. The company then decided to plead guilty.

Following the United States Supreme Court's 2001 decision in *Solid Waste Agency of Northern Cook County v. U.S.* (531 U.S. 159) ("SWANCC"), the defendant filed a writ of error *coram nobis* to correct errors of fact. The defendant argued that since the SWANCC held that isolated wetlands were not jurisdictional wetlands, it did not have to obtain a wetlands permit to fill in the wetlands. However, in *United States v. Wilson*, No. 01-4513, (4<sup>th</sup> Cir, 7/2/02), the Court of Appeals for the Fourth Circuit ruled that the conviction did not involve the so-called migratory bird rule but wetlands that were adjacent to tributaries of navigable waters.

### ***Vineyard Developer Receives Prison Term for Sediment Runoff***

A vineyard developer was sentenced to six months in jail and fined \$25,000 for allowing sediment from a construction site to erode into a stream. In *California v. Wilson*, (Cal. Super. Ct., No. MCR 364573), the defendant cleared ten acres of hillside to develop a vineyard. He failed to prepare a subsurface drainage system and did not develop a crop cover plan to control erosion. During the 1999 rainy season, large

quantities of sediment were carried into a creek where endangered fish lived.

**Commentary:** This action was brought under state law. EPA promulgated its Phase II stormwater regulations in 1999 requiring construction sites from one to five acres to control sediment runoff. In June, EPA proposed effluent limitation guidelines for active construction sites (67 F.R.42644, June 24,2002) Originally, EPA was considering requiring construction operators to treat 80% of the average rainwater striking impervious surfaces but did not include that requirement in the final proposed rule.

The proposal contains several options but does not establish numeric effluent limitations One option that would only apply to construction sites that have at least five acres requires construction operators design and install sediment controls, prepare a stormwater pollution prevention plan, conduct frequent inspections and certify that the controls are properly working. Another option would require operators of construction sites larger than one acre to inspect controls during active construction and certify compliance with the regulatory design criteria. The third option would not establish national design criteria but require contractors to comply with control measures established by the local permitting agencies.

The proposal does not establish permanent federal post-construction control requirements for residential or commercial developments. However, the Phase II rule required municipalities to establish their own post-construction control requirements such as detention ponds. Some developers use permeable parking lots, biological buffers or small wetlands to capture or hold stormwater so that it can slowly percolate into the ground. Without federal criteria,

municipalities would have to establish their own criteria to make sure the retention ponds are not undersized. Seven states and California have enacted their own numeric standards for stormwater controls.

### ***EPA Proposes Water Quality Trading Program***

EPA has proposed allowing point sources to trade pollution reduction credits to meet water quality standards (67 FR 34709, May 15, 2002). EPA hopes its Water Quality Trading Policy will provide states with more flexible and cost effective approaches to improving and maintaining water quality.

Under the proposed policy, industrial and municipal facilities that reduce pollution loads beyond the levels required by the most stringent technology could obtain pollution reduction "credit" that could be sold or traded to other sources discharging to the water body. For example, a landowner or a farmer could create credits by changing cropping practices and planting shrubs and trees next to a stream. A municipal wastewater treatment plant could then purchase these credits to meet water quality limits in its permit. The policy would allow trading between regulated and unregulated sources through watershed partnerships and programs developed by states and tribes.

### ***Dental Offices Are Third Largest Source of Mercury Contamination in Water***

Many purchasers of commercial properties and their lenders often view medical offices as low environmental risk operations. However, medical practices can generate a variety of hazardous wastes in addition to medical waste. A recent study conducted by Boston-based Health Care Without Harm illustrates the environmental problems that can be generated by a medical office.

According to the report, dental offices are a significant contributor of mercury contamination to surface waters. The report said that dental offices use approximately 40 tons of mercury each year, which is the third highest total in the nation after wire producers and manufacturers of electrical switches. Although many dentists use filtering systems to capture mercury before it is washed away, small particles of mercury can be washed down the drains during a tooth filling. The mercury can then

pass through the sewer system and be discharged into surface waters.

**Commentary:** Mercury is becoming to this decade what lead was to the 1990s. As a result, owners of commercial property and their lenders should determine during due diligence if tenant dental offices have adequate mercury handling and filtering procedures in place. If they do not, the borrower should be required to make sure that its tenants implement measures to prevent discharges of mercury into the sewer system.

### ***Motel Shut Down Because of Drinking Water Violations***

The Red Caboose Motel in Paradise, Pennsylvania was fined \$10,000 and ordered to close business until it corrected excessive levels of nitrates in the drinking water supply system.

The 47-room motel which is operated by Caboose Management Inc, has an on-site, public water supply system. The federal maximum contaminant level ("MCL") for nitrate is 10 milligram per liter (mg/l). However, monitoring tests consistently found nitrate levels between 25 mg/l and 30 mg/l with some samples as high as 70 mg/l. The state DEP issued a compliance order and obtained two court orders requiring Caboose Management to bring the nitrates levels down to the MCL. Caboose Management ignored the orders and the court held the firm in contempt and ordered the motel closed until it comes into full compliance with DEP's Order.

**Commentary:** Although nitrates are not considered hazardous substances, concentrations above 10 mg/l can result in blue baby syndrome in newborns and fetuses. Levels above 20 mg/l can interfere with the blood's ability to carry oxygen throughout the body, regardless of age.

During due diligence, drinking water samples should be collected for properties that have on-site drinking water wells. If the results exceed the MCLs established under the federal Safe Drinking Water Act, the property owner should be required to take corrective action to bring the contaminant concentrations below the MCL.

### ***EPA Amends SPCC Regulations***

EPA issued comprehensive revisions to its Spill Prevention, Control and Countermeasure ("SPCC") regulations (67

FR 47042, July 17, 2002). The new regulations become effective on August 17, 2002.

The revised regulations will apply to owners or operators of non-transportation facilities that store or use oil such as electrical substations, facilities containing transformers and certain hydraulic or manufacturing facilities. These non-storage systems do not necessarily have to be equipped with secondary containment so long as they have diversionary structures to prevent discharges of oil from reaching navigable waters. The geographic scope of the rule was extended from facilities that could discharge oil to navigable waters to facilities that could have oil discharges to shorelines and offshore waters.

In addition, the regulatory threshold for the SPCC rule was raised to facilities that have 1,320 gallons of aboveground storage capacity. The old rule also applied to facilities that had individual containers with capacities of at least 660 gallons. The revised rule contains a de minimis exemption so that only containers with a capacity at least 55 gallons or more are

counted when calculating the aboveground storage capacity.

Facilities with underground storage of at least 42,000 gallons are also subject to the SPCC rules. However, USTs regulated under a state or federal UST program or that have been permanently closed in accordance with the UST regulations will not be counted when calculating the underground storage capacity of the facility for SPCC regulatory threshold purposes.

The definition of oil under the revised rule is not limited to petroleum products. Facilities that store mineral oil, vegetable oil, synthetic oil, animal fats or grease, seed oil may be subject to the SPCC rules if they meet the regulatory thresholds.

**Commentary:** Some states require secondary containment for small aboveground storage tanks ("ASTs"). During due diligence, it is advisable to determine if ASTs must be equipped with secondary containment. Even where not required, secondary containment may be a best management practice for ASTs because of their location such as near floor drains to minimize the possibility that oil could be discharged into the environment.

## HAZARDOUS WASTES/USTS

### *EPA Issues RCRA Reuse Certificate for Voluntary Cleanup*

During the past few years, state environmental agencies have begun issuing no further action ("NFA") letters under their state superfund, voluntary cleanup and UST programs so that property owners can demonstrate that their sites have been adequately remediated. However, there has not been any comparable closure document under the RCRA program.

Inspired by these programs, EPA Region 6 recently issued the first "ready for reuse certificate" for the Sheffield Steel plant in Oklahoma. Another interesting aspect of this development was that the cleanup was performed under the state voluntary cleanup program ("VCP"). The facility entered the VCP after a 1997 EPA compliance-evaluation inspection suggested that hazardous constituents might be leaching out of clay-lined cooling ponds. After a five-year cleanup, EPA issued its novel

certificate confirming that environmental conditions at the site are protective for its current use and anticipated future uses as an industrial property. Unlike NFA letters, though, the certificate does not protect lenders or subsequent landowners from EPA future enforcement actions. The company has no current plans to sell the property but the certificate could help with refinancing.

**Commentary:** EPA issued its guidance for recognizing completion of corrective actions in 2001(66 FR 50195, October 1, 2001). The guidance indicated that the agency may issue a completion document after it determines the corrective action requirements of a RCRA permit or corrective action order has been satisfied. For facilities with RCRA corrective requirements in their permits, the permitting agency would modify the permit to indicate that the corrective action has been completed. If there are no other conditions in the permit, the expiration date of the permit could be moved up. At non-permitted facilities with facility-wide

corrective action, the completion may be acknowledged by terminating the interim status through the administrative procedures for denying permits. However, the regulatory agency may choose to use alternative terminology such as a "no permit necessary determination". Where the corrective action only involves a portion of a facility, a partial completion determination could be issued. For example, a facility that has completed closure at a SWMU but still conducting post-closure care at a HWMU would not have its interim status terminated.

Last year, EPA issued a memorandum "Comfort/Status Letters for RCRA Brownfield Sites" (February 5, 2001) authorizing the use of comfort letters for brownfield sites associated with TSD or generator-only facilities. The guidance document indicated that the letters may be used to facilitate cleanup or reuse of a brownfield site where there is a realistic perception or probability that EPA will initiate a RCRA cleanup and there is no other mechanism to adequately address the party's concerns. Examples of such letters include a letter indicating that corrective action is being or has been performed under supervision by a delegated state and that EPA intends to rely on the state to resolve any current or future closure or corrective action. Another type of letter is that corrective action has been performed or is about to be completed at the facility and that EPA does not anticipate further work will be required once the activities have been successfully completed. The last letter suggested by the guidance is that the property has not been identified as being subject to RCRA and therefore EPA does not anticipate initiating any response actions at the site.

#### ***EPA Grants Corrective Action Interim Authorization to 25 States***

Earlier this year, we discussed EPA's amendments to its Corrective Action Management Unit ("CAMU") rule. Because the 2002 CAMU amendments were generally more stringent than the 1993 CAMU regulations, regulated facilities faced the possibility of being subject to dual CAMU requirements if states authorized to administer the 1993 rule were not authorized to implement the 2002 amendments.

To avoid this potential disruption to the RCRA cleanup program, EPA recently

decided to grant interim authorization to the states that received final authorization for the 1993 CAMU rule. The 25 states that received interim authorization are: Alabama, California, Delaware, Florida, Georgia, Illinois, Indiana, Louisiana, Missouri, Nevada, New Mexico, New York, North Carolina, North Dakota, Oklahoma, Oregon, South Carolina, South Dakota, Tennessee, Texas, Utah, Vermont, Washington, Wisconsin, and Wyoming.

#### ***EPA Proposes Exempt Recycled CRTs From RCRA Regulation***

In past issues, we have discussed the environmental threat posed by the disposal of electronic equipment. Because this equipment contains a variety of toxic metals such as mercury, cadmium and lead, it is currently regulated as characteristic hazardous wastes under RCRA unless disposed by a household or a conditionally exempt small quantity generator ("CESQG").

To discourage the disposal of this equipment at municipal landfills and incinerators as well as to promote safe reuse and recycling of these products, EPA recently proposed to exclude used cathode ray tubes ("CRTs") from regulation under Subtitle C of RCRA unless they are disposed. The exemption would apply to CRTs that exceed the RCRA speculative accumulation limits so that CRTs could be stored indefinitely without becoming solid wastes.

EPA has consistently taken the view that materials used and taken out of service by one person are not wastes if a second person uses them for the same purpose without first "reclaiming" the material. Many CRTs are taken out of service by businesses and households because users are upgrading their systems. Many businesses and other organizations send used computers and televisions to resellers. Resellers often test CRTs to decide if the CRTs can be reused directly, if they can be reused after minor repairs, or if they must be sent for further processing or disposal. Under the proposed rule, used, intact CRTs that are sent to a reseller for resale, distribution or repair will be considered products "in use" and not solid wastes.

Used, broken CRTs sent for recycling would not be solid wastes if they are stored in an enclosed building, or stored

and shipped in a container that is designed to minimize releases of CRT glass to the environment. The packages must also be clearly labeled. However, broken CRTs destined for recycling could not be speculatively accumulated.

Sometimes manufacturers of computers and televisions send unused CRTs (usually off-specification CRTs) directly to glass processors who break the CRTs and separate out the glass components. The processor then usually sends the processed glass to a glass recycler or to another recycling facility such as a lead smelter. Under the current RCRA regulations, used CRTs sent directly to glass processors or other recyclers could be considered spent materials undergoing reclamation, and therefore be classified as solid wastes. Under the proposed rule, EPA would consider unused CRTs to be unused commercial chemical products and not solid wastes sent for reclamation.

Likewise, used and broken CRTs are sometimes sent to a glass processor who will intentionally break the CRTs to remove glass and clean coatings from the glass. Under the proposal, used and broken CRTs destined for glass processing would be excluded from the definition of solid waste if they are stored in an enclosed building or in a clearly labeled container that will minimize releases to the environment. In addition, all glass processing activities must take place within an enclosed building and no activities may be performed at temperatures that can volatilize lead. However, broken CRTs could not be speculatively accumulated.

Processed glass from used CRTs that is destined for recycling at a glass manufacturer or lead smelters would also be excluded from the definition of solid waste so long as the processed glass is not speculatively accumulated, and as long as it is not used in a manner constituting disposal. EPA believes that processed glass recycled in this manner qualifies for the variance from the definition of solid waste because this reclaimed material resembles a commodity.

Processed glass from used CRTs sent for recycling at a facility other than a glass manufacturer or a lead smelter would also be excluded from the definition of solid waste if the material was shipped and stored

in appropriately designed and labeled containers, and could not be speculatively accumulated.

Used CRTs that are sent for disposal or incineration would be subject to the RCRA hazardous waste program. If the used CRTs fail the lead TCLP test, they would have to meet applicable land disposal restrictions ("LDRs"). To meet LDRs, the CRT glass would have to be treated so the RCRA Toxic Characteristic Leaching Procedure ("TCLP") lead concentration does not exceed 0.75 milligrams per liter ("mg/l"). This concentration level is generally achieved by crushing and stabilizing the glass through the addition of chemicals which reduces the solubility of lead. Households or non-residential CESQGs that dispose of used CRTs would not have to comply with the hazardous waste management program of Subtitle C. A CESQG may not generate more than 220 pounds of hazardous waste in any one month. EPA estimates that 7 or 8 CRTs would weigh 220 pounds.

**Commentary:** CRTs are vacuum tubes that are video display components in computers and televisions, Oscilloscopes, appliances and automotive or medical equipment. CRTs are built from specialized glass that often contains lead. The average color computer monitor or television contains four pounds of lead. The University of Florida conducted a study to determine if CRTs exceeded the toxicity characteristic for lead. Using TCLP, the study found that leachate from CRTs had 22.2 mg/l which exceeded the TCLP concentration limit for lead of 5 mg/l. The other typical metals found in CRT glass did not exceed their TCLP limits. In addition, lead from monochrome monitors was below the TCLP limit. Flat panel displays generally do not contain any lead but may contain encapsulated mercury in small amount.

In 1992, EPA issued a memorandum stating that used whole circuit boards would be considered scrap metal when sent for reclamation and exempt from regulation under RCRA. In the 1997 LDR Phase IV rule (62 FR 25998, May 12, 1997), EPA excluded shredded circuit boards being reclaimed from the definition of solid waste provided they are stored in containers designed to prevent releases to the environment prior to recovery and provided they are free of mercury switches, mercury

relays, nickel-cadmium batteries and lithium batteries. In 1998, the agency subsequently clarified that the scrap metal exemption applies to whole used circuit boards that contain minor battery or mercury switch components and that are sent for continued use, reuse, or recovery (63 FR 28556, May 26, 1998). EPA indicated it did not intend to regulate circuit boards containing minimal quantities of mercury and batteries that are protectively packaged to minimize dispersion of metal constituents. However, the agency said that once these materials were removed from the boards, they would become a newly generated waste subject to a hazardous waste determination.

EPA is studying certain non-CRT electronic materials to determine whether they consistently exhibit a hazardous waste characteristic but said it was not aware of any non-CRT computer components or electronic products that would generally be hazardous wastes. If EPA determines that non-CRT components exhibit a hazardous waste characteristic, the agency use the same approach proposed for CRTs.

#### ***EPA Proposes to Regulate Mercury-Containing Equipment as Universal Waste***

EPA has also proposed to regulate spent mercury-containing equipment such as switches, barometers, meters, relay switches, manometers, temperature gauges, pressure gauges and sprinkler system contacts under its universal wastes rule. As a universal waste, the spent mercury equipment would be subject to more streamlined management requirements than those established under the RCRA hazardous waste program. Small Quantity Handlers of Universal Waste (accumulate less than 5,000 kilograms of universal wastes) would comply with less stringent management standards, labeling and marking requirements, accumulation time limits, employee training, release response, off-site shipment and export rules. Large Quantity Handlers of Universal Waste would also comply with notification and tracking requirements.

Because the proposed rule is less stringent than the RCRA hazardous waste requirements, delegated states would not be required to adopt the streamlined rule unless their standards for spent mercury equipment

are less stringent than the universal waste rule.

**Commentary:** EPA promulgated its universal waste rule in 1995 (60 FR 25942, May 11, 1995). To qualify as a universal waste, EPA must determine that the waste would qualify as a RCRA hazardous waste, is generated by a wide range of businesses, is generated by a large number of generators but in small volumes, regulation as a universal waste would encourage responsible stewardship, the risks posed by the waste during accumulation and transportation would be relatively low when compared to other hazardous wastes, the specific management standards are protective of human health and the environment, and management as a universal waste would increase recycling. Thus far, batteries, thermostats, lamps and pesticides are regulated as universal wastes.

#### ***USTs Pose Threat to Florida Drinking Water***

According to an EPA study, 4,000 drinking wells serving 17 million people in Florida are threatened by leaking USTs ("LUSTs"). EPA indicated that California had the most LUSTs but Florida had more threatened drinking water supplies because of its porous soil and shallow aquifers. Thus far, cleanups at 3,000 USTs Florida sites have been completed while cleanups are underway at another 5,000 sites. Approximately 10,000 sites are eligible for funding from the state UST Trust Fund and are awaiting cleanup. UST cleanups in Florida have been averaging approximately \$300,000 per spill.

**Commentary:** According to a recent GAO study, 36 states have a adequate funding for their UST Trust funds. However, 16 states have stopped accepting or are scheduled to stop accepting new reimbursement claims from UST owners. UST owners in those states will have to obtain their own insurance to cover their cleanup liabilities. 11 states already have cleanup costs that exceed their balance in their trust funds.

#### ***BP To Pay \$45 Million for Non-Compliance With UST Standards***

BP recently agreed to pay a \$21 million fines, \$4 million in investigation costs and spend \$20.8 million to upgrade USTs at 59 gasoline stations in California that had

been formerly owned by Atlantic Richfield Co. ("Arco"). BP will also monitor and inspect at more than 900 of its California gasoline stations.

The state attorney general brought a lawsuit under the state Unfair Competition Act. The state said that Arco stations continued to sell gasoline while other stations were forced to shutdown because they could not comply with the 1998 UST upgrade deadline. Arco had settled similar charges for stations in San Joaquin County in 1999. After BP merged with Arco in 2000, state and local officials began investigating the former Arco stations. The investigators discovered that Arco had failed to make the required upgrades at 59 stations, failed to disclose the violations to regulators and misrepresented work that was done.

The settlement does not affect pending local enforcement actions in Orange County or other jurisdictions throughout the state.

**Commentary:** The enforcement action emphasizes the importance of examining compliance issues when acquiring a business. Purchasers should not only verify compliance with the 1998 UST standards but also inquire about inactive tanks to determine if they were properly closed. In addition, they should seek assignments of rights to any reimbursements from state UST funds and verify that the USTs are eligible for reimbursements. Purchasers should not assume that newly upgraded or installed USTs do not pose a risk to the environment. Our July 2001 issue discussed a GAO report that found 30% of the newly installed or upgraded USTs were not maintained or operating properly and that 14 states traced petroleum contamination to upgraded or new tanks. Another 15 states reported that leak detection equipment was frequently turned off or improperly maintained.

### ***Brooklyn UST Operator Fined \$300,000***

Buy Rite Garage, Inc., Buy Rite Fuel Oil Corporation (Buy Rite) and Dennis Firpo were ordered to close ten USTs at a Brooklyn garage and fined \$300,000 for failing to comply with the 1988 UST deadline for upgrading USTs. Buy Rite and Firpo must close or upgrade four large tanks and conduct an assessment of the entire site. The order further requires that Buy-Rite

monitor all tanks at the facility and provide release detection for the tanks and piping systems.

### ***Illinois Amends UST Program***

In June, Illinois Governor George Ryan signed legislation that changes the methodology for performing UST corrective actions and increases reimbursements from the UST Trust Fund. Under Public Act 92-554, owners or operators will no longer be required to conduct a soil classification analysis. Instead, they will be able to use a risk-based analysis. Under the new procedures, UST owners/operators will be required to submit site investigation and corrective action reports, budgets and completion reports that will be prepared by Licensed Site Professionals.

The new law will also increase reimbursements from \$2 million to \$3 million for owners/operators with 100 or more USTs. For owners/operators with less than 100 USTs, the corrective action reimbursements will be increased from \$1 million to \$2 million. The reimbursement limit for each leak incident was also raised from \$1 million to \$1.5 million.

### ***NY Court Rejects Class Action for MTBE Litigation***

Plaintiffs seeking an injunction to force oil companies to remediate drinking water wells contaminated by MTBE will not be able to pursue their claims in a class action. In the *Methyl Tertiary Butyl Ether (MTBE) Products Liability Litigation*, (MDL No. 1358 Master File No. 00 Civ. 1898), a New York State judge ruled that the plaintiffs failed to meet the requirement of "typicality" under Rule 23(a)(3). The plaintiffs had hoped to pursue injunctive relief as a class and then bring individual damage claims. The judge also ruled that some plaintiffs failed to show that their well water had been contaminated or that there was an imminent threat of contamination.

The judge said that while the named plaintiffs made the same legal arguments as the proposed class, their claims did not derive from the same course of conduct because the contamination of their wells came from factually unique set of circumstances such as a burst pipeline or a leaking container.

The judge also indicated that she had serious concerns the named plaintiffs could adequately represent the claims of the

absent class members because none of the named plaintiffs claimed personal injury. Instead, they complain of bad tasting or bad smelling water and had already received assistance in the form of alternative water sources, bottled water or filtration systems. The court was concerned that subsequent courts would preclude absent class members from bringing personal injury claims

**Commentary:** According to a recent GAO report "MTBE Contamination from Underground Storage Tanks", the full extent of MTBE contamination is unknown. While 44 states now test for MTBE at UST sites, only 24 states routinely analyze drinking water for MTBE. Because MTBE does not adsorb to soil particles as much as other gasoline constituents and more easily dissolves in water, many states admitted that their UST investigation procedures may not

detect the presence of MTBE. Those states may have to require more groundwater wells to determine if MTBE is present or migrating off the site. 37 states indicated that they use the same methods to remediate MTBE as other gasoline constituents. However, 16 states reported that the presence of MTBE increases the cost and delays the progress of UST cleanups. 10 states indicated they have reopened previously completed cleanups because MTBE was subsequently discovered.

## TOXIC SUBSTANCES

### ***Recycling Pleads Guilty to Illegal Disposal of Fluorescent Lights***

The owner of a recycling company was sentenced to 18 months in prison and ordered to pay more than \$280,000 in restitution to victims of a fraudulent fluorescent recycling scheme. The defendant owned and operated Consolidated Recycling Inc. (CRI), a New Hampshire firm that purported to be in the business of recycling fluorescent bulb and lighting ballast waste. CRI accepted light bulb and light ballast wastes that contained mercury and PCBs from school districts and government agencies in Colorado, New York, North Carolina and Ohio. He falsely claimed that CRI had the equipment to recycle the wastes but instead stored or abandoned wastes at several locations in New Hampshire and Massachusetts.

### ***DC Circuit Invalidates PCB Remediation Guidance***

The U.S. Court of Appeals for the District of Columbia invalidated an EPA guidance document for remediating PCB-contaminated wastes. In *General Electric Co. v. EPA*, (D.C. Cir., No. 00-1394, 5/17/02), the court held that EPA's "PCB Risk Assessment Review Guidance," issued in 2000 was essentially a rulemaking since

the agency made its requirements binding on responsible parties. As a result, the court said the guidance was a rule that was required to undergo notice and comment

### ***Chemical Waste Management Fined for Improper Handling of PCBs***

Chemical Waste Management, Inc. ("CWM") was assessed \$78,475 for illegally disposing 180 large capacitors containing PCBs at its Model City, New York landfill during the fall of 2000.

The PCB regulations require PCB-capacitors to be incinerated. However, CWM buried three steel boxes containing the capacitors at its landfill. Under its PCB Disposal Approval, CWM was required to open containers and inspect their contents prior to disposing of a waste shipment in its landfill. CWM reported the possibility of the violation almost two months after the material.

CWM also failed to record the accurate location of the containers in the landfill, which made recovery of the capacitors difficult. As a result, it spent more than \$460,000 to determine the exact location where the steel boxes were buried.

As a condition of the settlement, CWM voluntarily removed the capacitors

and shipped the large PCB capacitors to an incinerator facility. CWM also agreed to make changes in its PCB management and acceptance protocol at its Model City facility to prevent such violations in the future.

In addition to the improper disposal of the PCB capacitors, CWM was also fined

for illegally exporting PCB waste to Canada. The exported waste has been returned to the Model City facility and is awaiting proper disposal.

## SUPERFUND/BROWNFIELDS

### *EPA Issue New PPA Guidance*

In prior issues, we have examined the scope of the Bona Fide Prospective Purchaser ("BFP") defense that was added to the Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA) by the Small Business Relief and Brownfield Revitalization Act, Public Law 107- 118 ("2002 CERCLA Amendments"). Because of this defense, there had been much speculation over whether EPA would continue to issue Prospective Purchaser Agreements ("PPAs"). EPA put an end to the suspense in late May when it published its new PPA guidance.

In its *"Bona Fide Prospective Purchasers and the New Amendments to CERCLA"*, EPA reiterated its long-standing policy to not become involved in purely private real estate transactions. The agency said that the BFP defense would make it unnecessary for private parties to obtain PPAs in most cases. In addition, EPA said it believed that the BFP defense will enable parties in a transaction to avoid significant costs associated with negotiating PPAs and will no longer have to delay their deals while waiting for EPA to approve a PPA.

However, the guidance did recognize two instances where the public interest might be served by entering into PPAs or some other form of agreement. The first instance would be when there is likely to be a significant windfall lien and the purchaser needs to resolve the lien prior to secure financing. EPA indicated where a BFP and the United States could resolve a windfall lien claim in advance of the purchase of the property, an agreement might be limited to a settlement of the windfall lien claim. EPA said it was its belief that Congress intended the BFP to eliminate the need for most PPAs. Therefore, settlement of the windfall lien claim may be limited to that one issue. The agency also

recognized that it was not necessary to enter into an agreement everytime a party acquiring contaminated property is concerned about managing liability. EPA said its "Policy on the Issuance of EPA Comfort/Status Letters" was designed to help the public better understand the environmental status of certain properties and the likelihood that EPA would become involved at the site.

Regional offices could also consider entering into a PPA where necessary to ensure that the transaction will be completed and the project will provide substantial public benefits such as performance of a cleanup, reimbursement of EPA response costs, creation of jobs, revitalization of long blighted property, or promotion of environmental justice.

The guidance provided some examples when a PPA might be appropriate for this second condition. One situation was when the facility has not been remediated, there is no viable PRP who can be required to timely conduct the cleanup and no potential developer is willing to undertake the entire cleanup in order to develop so that the facility might sit idle for years. Another circumstance is when a purchaser has committed to perform significant cleanup as part of the redevelopment and is concerned about its potential liability as an owner or operator of the facility. The other illustration in the guidance was when EPA has commenced an enforcement action against the primary PRPs for the site and there is a very real possibility that the purchaser may be named in a contribution action. The guidance indicated that EPA is not prohibited from entering into a settlement with a purchaser after it has acquired property and otherwise qualifies as a BFP but is threatened with a contribution action.

EPA said it was committed to removing liability barriers to redevelopment of property. However, it was the agency's

hope and expectation that most brownfield transactions would now move forward without the need for EPA involvement.

**Commentary:** During the past three months, EPA announced it had agreed to enter into a number of PPAs. These agreements were negotiated prior to the issuance of the new PPA guidance. Two were negotiated after the passage of the 2002 CERCLA Amendments.

The Utah Transit Authority ("UTA") PPA was interesting because it contained new language incorporating one of the provisions of the 2002 CERCLA Amendments. In this agreement, UTA planned to acquire a 150-mile long and 20-foot wide railroad corridor from the Union Pacific Railroad. The railroad corridor runs through areas that were used for a variety of industrial operations. UTA plans to use the corridor to construct an above-grade light-rail system for the Salt Lake area. In exchange for the covenant not to sue, UTA agreed to provide EPA access to the Property, characterize soil that will be excavated to construct the "light-rail" system, and to properly handle or dispose of contaminated soils. UTA was not required to characterize areas of the site that are not to be disturbed during the construction of the light rail system nor remediate groundwater.

PPAs usually require the purchaser to exercise due care regarding existing contamination at the site. However, this PPA requires UTA to exercise "appropriate care" as described in the new legislation. UTA was not required to reimburse EPA any past costs. However, if it fails to comply with the terms of the PPA, it will be liable to EPA for litigation and enforcement costs and any expenses to bring the site into compliance.

The Leggett & Platt, Inc. ("L&P") and Sterling Steel Company, LLC ("Sterling") PPA also referred to the 2002 CERCLA Amendments. This agreement involved portions of the former Northwestern Steel and Wire Company ("NWSW") site in Sterling, Illinois. NWSW filed a chapter 11 bankruptcy petition and ceased operations at the site in May 2001. After performing Phase I and Phase II ESAs, the purchasers notified EPA in January after the 2002 CERCLA Amendments became effective that they wanted to acquire 144 acres of the 700-acre site to renovate and restart operations at two of the plants. The purchasers agreed to

remediate recognized environmental conditions identified during their due diligence, including removal of sludges, and drums, upgrading the groundwater treatment system, and construction of a concrete cap. For tasks not specifically set forth in the PPA, the purchasers would have to obtain a NFA letter from the state showing that they complied with the state's risk-based cleanup standards. In exchange for this work, EPA agreed to provide the purchasers with a covenant not to sue under both CERCLA and RCRA 7003 and contribution protection. While the PPA referred to the 2002 CERCLA Amendments, the "due care" language was not changed. The purchasers were not required to reimburse EPA any past costs. However, if they fail to comply with the terms of the PPA, it will be liable to EPA for litigation and enforcement costs and any expenses to bring the site into compliance.

The PPA for the Sharon Steel Superfund site in Midvale City, Utah was a good illustration how PPAs may be used to preserve open space and institutional controls must be taken into account for future development. In this agreement, thousands of tons of tailings had been left at the site when a milling operation ceased operations in 1971. EPA completed a response action in 1999 which consisted of construction of a cap. The 500-acre site is located along the Jordan River and interrupted several miles of bike and hiking trails. The current landowner had received several offers from developers but agreed to donate the site to allow the trail network to be connected. The City of Midvale entered into a PPA to acquire permanent public easements and access rights across operable unit ("OU") 1. The City plans to use funds from the TEA-21 program to construct an overpass to allow the trails to be extended onto the property and to construct a pedestrian and bicycle trail. The City received covenants not to sue from EPA and the Utah Department of Environmental Quality ("UDEQ") for existing contamination and will also receive contribution protection. In consideration for these covenants not to sue, the City agreed to perform operation and maintenance ("O&M") activities including periodic inspections of the cap and repair of asphalt surfaces, landscaped areas, sidewalks, curbs and gutters. The city must also submit annual reports to EPA and

the state DEQ. The city will have to prepare an O & M plan for approval by EPA and cannot begin any construction until the O & M plan is approved. The annualized value of the O&M activities is estimated to be \$22,505 for the overpass and \$4,938 for the trails. If the city fails to comply with the terms of the PPA including the O & M plan, it will be liable to EPA for litigation and enforcement costs and any expenses to bring the site into compliance.

The New Jersey Transit Corporation ("NJT") agreed to enter into a PPA to lease five acres of the 200 acre Roebling Steel Superfund Site in Florence Township. The property is currently owned by the local township but was formerly used by a steel wire and cable manufacturer until 1982. EPA performed response actions for OUs 1-4 and is currently performing an RI/FS at OU 5. NJT plans to build a light rail station and parking lot at the portion of the site it plans to lease. In exchange for the covenant not to sue and contribution protection, NJT agreed to construct an asphalt and soil cap, install stormwater management and erosion controls and install perimeter fencing. NJT will also be responsible for the long-term O & M of the cap, erosion controls and fencing. Contaminated soil that is excavated during the construction may be redeposited at the site and placed under the cap. The PPA contains an unusual insurance provision where NJT is required to maintain adequate general comprehensive liability, auto liability and workers compensation insurance with EPA named as an additional insured.

The New Jersey Department of Environmental Protection ("NJDEP") and the Township of Kingwood, New Jersey ("Township") entered into a PPA for the DeRue Chemical Company Superfund Site in Kingwood Township, New Jersey. A chemical storage facility was formerly located on the 8.4 acre site. EPA completed a soil cleanup in 1998 and is currently conducting a groundwater investigation at the Site. The Township obtained title to the Property following tax foreclosure actions in the 1990s and now operates a park. NJDEP will purchase one of the parcels and the Township will convey a conservation easement to NJDEP for the two remaining parcels. NJDEP and the Township will also impose institutional controls on the Property and allow EPA access for remedial activities.

If NJDEP or the Township sell their parcels for a purpose other than conservation, they will be required to reimburse EPA for its past response costs.

A local development corporation entered into a PPA for the Franklin Smelting Site in Philadelphia. EPA had performed removal actions at this site from 1998-2000. The PIDC Local Development Corporation held a mortgage on the property and planned to foreclose. After taking title, it intended to sell two of the three parcels to an entity that planned to conduct light iron shredding and scrap metal recycling operations. In exchange for the covenant not to sue and contribution protection, the non-profit agreed to reimburse EPA \$5,000 for its past response costs, provide access to EPA to perform response actions and the other customary obligations usually contained in PPAs. PIDC also agreed to maintain documents relating to site investigations and operations at the site for ten years.

#### ***Purchaser of Contaminated Site Shares Sales Proceeds With EPA***

EPA agreed to provide a covenant not to sue to a purchaser acquiring a contaminated site and the assets of a PRP who was the responsible for the contamination. Though not captioned as a PPA, the agreement served the same purpose. In this matter, Industrial Container Services, LLC ("ICS") and Industrial Container Services-FL, LLC ("ICS-FL") agreed to purchase 14 acres of the 40-acre Zellwood Groundwater Superfund Site located in Zellwood, Florida. ICS-FL intends to operate a drum reconditioning facility at the site. Prior to the sale of the property, ICS-FL entered into a service agreement with the PRP and owner of the site, IFCO-ICS-Florida, Inc., to purchase and recondition drums. The PRP was obligated to implement the remedy. In exchange for the covenant not to sue, the purchasers agreed to deliver the purchase price of \$114,419 to EPA and to maintain financial assurances of \$1,280,956 to guarantee performance of the remedy. The agreement allows the purchasers to reduce the amount of the financial assurance periodically equal to the remaining estimated costs to complete the cleanup. The purchasers must also comply with any institutional controls imposed at the site.

#### ***Consent Decree Modified to Reflect***

### ***Less Costly Remedy***

The first decade and half of the Superfund program was often plagued with inconsistent remedy decisions. This resulted in some sites having more costly cleanups than other similarly-situated sites. As part of its Superfund reforms in the mid-1990s, EPA tried to add consistency to the remedy selection process by developing presumptive remedies for certain kinds of contaminants and creating a Remedy Review Board to examine early remedy decisions made at the more mature Superfund sites.

A recent amendment to a consent decree illustrates how these procedural reforms can result in significant cost savings for PRPs. In *United States v. Scovill, Inc.*, EPA agreed to change the groundwater remedy from pump and treat system to a Permeable Reactive Subsurface Barrier ("PRSB") and installation of a surface cap. The original remedy had been selected before the agency issued its guidance on using land use when selecting remedies. In addition to the change in the groundwater remedy, the successor to the ordered party agreed to undertake certain unanticipated work at the site in exchange for a credit against future oversight costs incurred by the EPA.

### ***EPA Awards Brownfield Grants***

EPA awarded 80 new or supplemental Brownfield Assessment Demonstration Pilot ("BADP") grants totaling \$14.6 million in May. 38 of the grants totaling \$7.95 million were for new pilots while 42 of the grants totaling \$6.65 million were supplemental grants for existing pilots. Since inception of the assessment pilot program, the agency has awarded more than \$280 million in pilots.

Meanwhile, EPA also awarded 40 USTfields grants of up to \$100,000 each to 26 states and three tribes to assess and remediate properties contaminated from leaking underground storage tanks ("UST"). EPA has now awarded 50 USTfields pilots.

### ***Report Finds Many Schools Located Near Hazardous Waste Sites***

A recent report by the Childhood Proofing our Communities Campaign found that almost 1,200 public schools in five states were within a half-mile of a federal or state superfund site. In those five states,

over 600,000 children attend classes near the contaminated properties.

According to the report, the average public school building is about 42 years in age. In New York alone, 235 schools in 39 counties are reported to be within a half-mile of a contaminated site.

### ***Many Shopping Centers Qualify as "Greyfields"***

We have all heard about Brownfields and Greenfields. Within the last few months, a new term "Greyfields" has emerged that refers to obsolete and non-profitable retail sites located in cities and older suburbs that have fallen into disrepair and do not generate enough revenue to justify their continued use. Developers and lenders are reluctant to upgrade the older retail centers because they have been impacted from prior operations such as service stations and dry cleaners.

### ***Pennsylvania Announces Brownfield Inventory Grants***

The state DEP has awarded 31 Brownfield Inventory Grants Program to local governments, economic development agencies, and other organizations to cover the costs of locating and researching sites that could qualify for the state Land Recycling Program. Grant recipients receive \$1,000 for every site listed on PA SiteFinder with a maximum grant of \$50,000 per recipient. Thus far, 31 recipients have earned \$285,000 by placing brownfield sites the inventory.

350 state brownfield sites have been listed on the PA SiteFinder, a website that compiles property information, financial assistance and other technical assistance in one user-friendly place to help guide buyers and sellers through real estate transactions.

Prior to PA SiteFinder, sellers of brownfield properties had to rely on traditional marketing strategies to attract buyers. Strategies such as advertising were often costly and did not always reach the intended target audience. Potential buyers, on the other hand, had to do a significant amount of legwork to identify available brownfield properties. PA SiteFinder's services and convenience help facilitate brownfield remediation and offer a clear road

to redevelopment. Thus far, 25 sites have been sold through the website

**Commentary:** Pennsylvania also announced changes to its Act 2 Technical Guidance Manual that will make it easier for developers to rehabilitate sites. One of the key changes is to allow municipal authorities to designate groundwater as a non-use aquifer. This pre-certification could speed the redevelopment of brownfields like industrial parks. Previously, a developer needed to perform extensive and costly tests during rehabilitation of a site to certify groundwater at the site was a non-use aquifer. Another key change in the new manual clarifies the relationship between waste management and land recycling.

#### ***New Law Changes Liability***

##### ***Scheme for Pennsylvania***

##### ***Superfund Law***

The Pennsylvania legislature recently approved S.B. 1089 that dramatically alters the state's comparative negligence statute by abolishing joint and several liability for defendants. Under the measure, the state would retain the doctrine of joint and several liability if a defendant has been held liable for at least 60% of the damage award for a release or threatened release of a hazardous substance under Pennsylvania's Hazardous Waste Cleanup Act. However, in cases in which

damages for negligence are apportioned among multiple defendants, each defendant would be responsible for paying only its proportionate share of the total dollar amount awarded as damages.

#### ***Ohio To Award Brownfield***

##### ***Grants***

The Ohio Department of Development will award \$40 million in assessment and cleanup grants under its revamped brownfield program. Each of the 27 recipients will receive up to \$3 million.

**Commentary:** EPA found Ohio's eight-year-old Voluntary Action Plan ("VAP") inadequate because of insufficient oversight. VAP cleanup teams were not required to provide information about site contaminant characterization or cleanup programs until work was finished. As a result, EPA never certified the plan. The modified program gives for enhanced public participation earlier in projects. In addition, each program team must have a state-certified contractor who will ensure that the plan and the work comply with state standards.

## **ENVIRONMENTAL CASES INVOLVING CORPORATE AND REAL ESTATE TRANSACTIONS**

#### ***Borrower Not Liable to Bank For Failing To Disclose Contamination***

A California appellate court denied a cross-claim for fraud claim filed by a bank against its borrower for failing to disclose the existence of contamination at a site that secured a \$250,000 loan.

In *Quinn v McCoy* (No. A091124, Cal. Ct.App, June 14, 2002), the plaintiff used the loan proceeds to purchase a former general store that had underground

storage tanks and had gone out of business in 1977. The plaintiff acquired the property in March 1990 at an auction conducted by Marin County to collect back taxes. A 1989 newspaper article had discussed the upcoming auction and indicated that prospective purchasers were being cautioned about the presence of toxic materials in the soils at the site. The bank did not conduct any due diligence and did not request the borrower to disclose any contamination in its loan application. However, the deed of trust contained an

express representation that the borrower did not know of any environmental conditions at the property.

The loan was to expire in December 1991 but the bank agreed to extend the term until April 1992. In March 1992, the bank learned from an appraiser that the property was contaminated. The loan officer sent a letter to the plaintiff attached the 1989 newspaper article and asked the borrower to discuss the environmental issues. After the bank agreed to extend the loan to December 1992, the plaintiff responded that it had not heard anything from the regulators regarding the contamination and had assumed the matter had been resolved.

The bank declined to extend the loan and when the borrower could not obtain further financing by March 1993, the bank ordered a phase I ESA in anticipation of foreclosure that indicated the site was contaminated. In December 1993 when the foreclosure was scheduled, the bank received an estimate that the site cleanup would cost \$580,194. The bank delayed foreclosing proceedings several more times and extended the loan in exchange for monthly interest payments until February 1995.

In March 1995, the plaintiff agreed to sell the property to the defendant for \$275,000 and to remediate the site. However, he lacked the resources to pay for the cleanup. In February 1996, the defendant offered to purchase the property at a significant discount and remediate the site himself. When the plaintiff rejected the offer, the defendant approached the bank about purchasing the note and deed of trust for \$75,000. He asked the bank not to disclose the purchase of the note because the plaintiff might file for bankruptcy and prevent the foreclosure sale. In June 1996, the defendant purchased the note, the bank foreclosed on the property and title reverted to the defendant.

The plaintiff filed a wrongful foreclosure action against the purchaser of the note and the bank for failing to notify it of the sale of the promissory note. The bank filed a cross-claim for failing to disclose the contamination. Ignoring the express representation in the deed of trust, the trial court denied the bank's cross-claims because the bank had failed to inquire about the borrower's knowledge of the site

conditions and because it had restructured the loan for three years after learning of the contamination. On appeal, the court said the cross-claim for fraud had been filed more than three years after the bank had learned of the contamination and the borrower's failure to disclose what it knew. Therefore, the claim was barred by the statute of limitations.

**Commentary:** This case illustrates the importance for banks to perform due diligence prior to issuing a loan and to develop workout and foreclosure procedures for contaminated property. In this case, the bank was so concerned about foreclosing on contaminated property that it failed to examine the legal remedies that were available to it and allowed the statute of limitations to expire.

### ***Debtor-In-Possession Prohibited From Abandoning Property***

In our last issue, we discussed how some brownfield developers believe they can use the Bankruptcy Code (the "Code") to avoid liabilities associated with contaminated properties. In that article we explained that developers seek to purchase contaminated property "free and clear of any liens or interests" under Code section 363(f) to cut off liability for pre-existing contamination and then use the new Bona Fide Prospective Purchaser Defense to eliminate their liability as a current owner of contaminated property.

Another strategy that has been rejuvenated since the CERCLA 2002 Amendments is the power of the trustee to abandon property that has no value to the debtor. Under this scenario, the debtor could sell off profitable assets to reorganize its business and abandon contaminated properties to a creditor who would then utilize the Bona Fide Prospective Purchaser defense to avoid liability and find a third party to develop the site.

Code section 554 authorizes a trustee to abandon property that is "burdensome and of inconsequential value" to the bankruptcy estate. Debtors-in-possession ("DIP") in a chapter 11 reorganization proceeding can also abandon property. While the abandonment property is broad, it is not unlimited. The United States Supreme Court ruled in *Midlantic National Bank v. NJDEP* (474 U.S. 1986) that a trustee court may not abandon of property that would violate laws that are reasonably

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designed to protect human health and safety. The ruling went on to say that a bankruptcy court may not authorize abandonment without formulating conditions to make sure that the abandonment would not pose an immediate and identifiable harm to public health and safety.

Immediately after the Midlantic decision, a number of bankruptcy courts refused to approve abandonment. However, the overwhelming majority of decisions since the mid-1990s have not only authorized abandonment but have often done so without imposing any conditions on the abandonment. In nearly all these cases, there was some level of contamination and frequently the contamination was above cleanup levels. However, because the state had either not taken any action to abate the contamination or bring an enforcement action against the debtor, or because the debtor lacked sufficient funds to remediate the site, the court authorized the abandonment.

Abandonment is a more viable option when there is a chapter 7 or chapter 11 liquidation proceeding since the property will usually be abandoned to an insolvent debtor or a creditor. However, abandonment is more problematic in a chapter 11 reorganization since after the bankruptcy case is completed, the estate of debtor will be merged with the reorganized company. Thus, property abandoned in a chapter 11 reorganization to the debtor would end up

owned by the reorganized property.

This was the situation facing the bankruptcy court in *In re ABC-NACO Inc* (No.01 B 36484). In this case, a manufacturer of railcar undercarriages sold substantially all of its assets. The sale specifically excluded two potentially contaminated properties and the DIP moved to abandon these properties where it had discontinued operations and had vacated. The debtor said it would not be seeking to use these properties, had no equity in the parcels and was incurring ongoing expenses to maintain them. As a result, the properties were burdensome and of inconsequential value to the estate. The lender holding mortgages on these sites had information about environmental conditions at these three facilities but refused to provide them to EPA. As a result, EPA objected to the abandonment.

The court denied the motion on the grounds that as a DIP, the debtor was not entitled to relief because the debtor and the reorganized company were the same entity. The debtor filed a motion for reconsideration and the court decided to allow the debtor to establish that the property did not pose an imminent and identifiable harm to public health and safety. The court also indicated that abandonment would have to be conditioned on providing EPA access to the properties to investigate environmental conditions.

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We also offer a seminar "Environmental Problems in Business Transactions" which has been approved by the New York Continuing Legal Education Board as an Accredited Mandatory Continuing Legal Education ("MCLE") Program. The fee for the seminar is \$20 per credit hour. A course book with transactional forms is included with the seminar. The course book may be purchased separately for \$95. The seminar can be conducted at your office or at periodic department meetings that you might organize over the course of the year. If you are interested in this seminar or purchasing the course book, please

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contact Lawrence Schnapf.

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