SCHNAPF ENVIRONMENTAL REPORT

A Newsletter Covering Recent Environmental Developments and Caselaw

September/October 2002 Vol. 4, Issue 5

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DUE DILIGENCE/ AUDITING/ DISCLOSURE/ ENFORCEMENT

States Cutting Back of Enforcement

In our March 2002 issue, we reported on a study by the Environmental Council of States ("ECOS") that found that states administered nearly 80% of the federal environmental programs. ECOS also determined state environmental agencies accounted for 70% of all formal administrative enforcement actions brought between 1995 and 1999. Now with 47 states facing budget deficits, a new ECOS survey has found that 30 states have had to reduce their environmental budgets. Eight more states did not increase spending for environmental programs.

According to the ECOS study, state spending on environmental programs has dropped by about 3.7%. The average cut was about $6.8 million per state. One state agency alone lost $70 million in fiscal year 2003. Last year, 42 states slashed their environmental budgets by an average of $6.5 million per state. 74% of the spending reductions were targeted at general, unallocated funds. These budget reductions were largely accomplished by imposing freezes on hiring and promotion, travel restrictions and reductions in new contracts and purchases.

ECOS did identify specific programs that have received budget cuts. States spend the largest percentage of their environmental budgets on water programs so it was not surprising that water quality programs were targeted for the largest budget reductions. ECOS identified 32 water quality programs slated for cuts including groundwater monitoring, oversight of aquifer water quality permits, wetlands protection, shore protection, monitoring of non-TMDL sources including non-point source runoff from concentrated animal feeding operations ("CAFOs"). Other programs suffering budget cuts included eight clean air programs, seven hazardous waste programs, three drinking water programs and three pollution prevention programs.

None of the 42 states participating in the ECOS study reported cuts to enforcement programs. One way that state regulators were dealing with smaller budgets was to adopt more targeted enforcement and shift to a multi-media approach. Under this approach, separate air, water, hazardous waste enforcement programs are reorganized into one enforcement unit.

Commentary: The budget cuts come as many state environmental agencies are facing increased demands on their resources because of new homeland security requirements. After the September 11 terrorist attacks, state agencies have assumed responsibility for safeguarding local water supplies safe but have not been given the additional resources to meet these responsibilities.

Banks Starting to Add Mold to Due Diligence Requirements

Anecdotal evidence from environmental consultants indicates that many financial institutions are adding mold to their due diligence requirements. A recent study in ESA Report published by EDR estimated that 10% of the largest mortgage lenders had developed there own scope of work for mold investigation.

The banks are taking a variety of approaches to the mold investigation. Some are asking that mold be addressed in Property Condition Assessments ("PCA") while those who do not normally order PCAs are using ESAs to evaluate mold. Many only require visual observations and do not require sampling before mold remediation.

Lenders are increasing using the NYC "Guidelines on Assessment and Remediation of Fungi in Indoor

Environments". For example, the NYC guidelines allow building maintenance workers to remediate mold infestation less than 30 square feet. Many lenders will only become concerned if the mold exceeds this threshold though they may want the borrower to covenant that it will abate the mold. A few lenders also require the borrower to establish an O & M approach where tenants are advised to perform regular inspections and notify landlord if mold is suspected.

In addition to banks, there appears to be a growing demand for mold assessments from owners of multi-family properties as well as commercial buildings. One reason for the heightened interest is that property owners are having increasing difficulty obtaining insurance with mold coverage and are concerned about their exposure to lawsuits.

Commentary: Mold is often a problem at residential property because of extensive piping. While there has been less litigation associated with commercial buildings, the risk of widespread mold contamination is higher in commercial buildings because the powerful HVAC systems can distribute spores throughout the buildings. For example, the new $95 million dollar Hilton Kalia Tower was recently shutdown because of mold. The Kalia Tower is one of six hotels comprising the Hilton Hawaii Village. All 453 rooms in the one-year-old hotel representing 13% of the rooms in the entire hotel complex have been closed indefinitely. A housekeeper discovered the mold and the hotel estimates the mold abatement costs will be $10 million. Mold was also detected in the corridors of the 264-room Lagoon Tower but that hotel was not closed.

Because of the high standard of care imposed on hospitality facilities, the economic losses that can occur if they are forced to shutdown and the possibility of stigmatization, it is advisable that pre-acquisition due diligence include mold sampling when water damage is observed. Management agreements should contain provisions for periodic mold inspections and describe preventative maintenance obligations that should be performed to minimize the possibility of mold growth.

Many landlords are increasingly including inspection requirements in multi-family leases where the tenant is required to periodically check certain areas for mold growth and required to notify management of any mold that is found. If the tenant fails to comply with these lease obligations, management will consider the tenant in breach of its lease and assert that the tenant negligently maintained the premises.

In commercial lease, landlords are amending their duty to repair clauses. The newer leases are giving landlords broad rights to inspect for obvious signs of mold. Even where the tenant may have such an obligation, the landlord may retain a right of entry to address mold issues before they become widespread.

Mold issues can be particularly sticky in condominium or co-ops. The documents should indicate when the maintenance and repair obligations of the condo association or co-op board end and the tenant/unit owner begin. If the unit owner or co-op tenant fails to comply, the association or board should have the right to enter units to take abatement actions. Some associations are requiring unit owners to periodically perform mold inspections or at least have the power to condition a sale of a unit on the completion of a mold inspection.

Report Finds No Link Between Mold Exposure and Neurological Impairment

A paper presented at a mold conference hosted by Georgetown University Department of Pharmacology and the International Center for Toxicology and Medicine concluded that there was no scientific basis that breathing mold spores or mycotoxins in homes or commercial offices can result in neurological impairment.

According to Dr. Paul Lee of the Health Education Services, the one study most often cited to support the neurotoxicity of mold exposure was so flawed it could not be considered a scientific study. Dr. Lee said the report was not peer reviewed, did not have any control group, did not administer a standardized test to all participants, alternative exposures were not investigated and the paper only reported data from tests that were more likely to produce the results desired by the author. In the only peer-reviewed study, Dr. Lee said the subjects exposed to mold actually performed better on cognitive tests than the control group. He said there was no established pattern of neurological or psychological syndromes or

diagnosable mental disorders associated with inhalation of mycotoxins or mold spores.

Dr. Lee's report indicated that studies of the general adult population commonly produce high rates of mild brain injury or psychological symptoms. He also said there were empirical studies that have documented discrepancies between patients who pursued litigation and those who were not seeking compensation. Dr. Lee said these studies show that many plaintiffs are more susceptible to suggestions that they have been injured and will tend to over-interpret or become anxious about symptoms that the general public tends to view as temporary "symptoms of life." He said that studies have shown that litigating patients report nearly twice as may symptoms as non-litigating patients. He said that litigating patients also tend to view their pre-injury health to be much better than those in control groups.

Heating Oil Tanks and Phase I Audits

The federal program does not regulate heating oil USTs used to heat the premises where the UST is located. The vast majority of states follows the federal approach and do not regulate these USTs. However, approximately 15 states have established regulatory programs for heating oil tanks. These state heating oil tank programs may not necessarily impose the full range of the UST regulations on the USTs. For example, some states that regulate heating fuel USTs will only require owners and operators to comply with the release reporting and corrective action requirements while others will also require compliance with the UST design standards.

Some of these states only regulate heating oil tanks above a certain size. For example, New York regulates fuel oil tanks with a capacity of 1,000 gallons or more while the New Jersey threshold is 2,000 gallons and Connecticut is 2100 gallons. Other states such as Delaware, Maine, Maryland, Massachusetts and Montana regulate all heating oil USTs regardless of size.

Because of the confusion over the requirements for heating oil tanks, many property owners may have closed or abandoned regulated tanks without complying with the UST closure requirements. For example, a property owner may fill an oil tank with sand without taking samples to determine if the tank had impacted the soil or groundwater at the site. As a result, it is important for purchasers to determine if heating oil tanks were previously used at the site and if they were subject to the state UST program. If the tanks were not exempt, the purchaser should determine if the tanks were properly closed. If the tanks were not closed in accordance with state requirements, the purchaser could become responsible for complying with the closure requirements after it takes title to the property.

Even where heating oil tanks are exempt from the state UST program, the tanks might be subject to local government or fire marshal closure requirements. Purchasers should also review the registration and closure requirements of local jurisdictions as well.

Florida Study Identifies Causes of Dry Cleaner Contamination

In 1992, a California study concluded that the primary cause of drycleaning solvent contamination was the discharge of PCE-saturated contact water into sewer lines and septic systems. Now, a Florida study has identified other causes of dry cleaner contamination that may change the way consultants evaluate impacts from dry cleaner operations.

According to the state study, nearly 40% of reported spills was from equipment failure attributable to leaking door gaskets, pump seals, joint gaskets, ruptures of pipes and hoses, failed hose clamps and pressure valves. Another common equipment leak was failure of cartridge filters because of excessive pressure from a buildup of soil, water repellants or fabric finishers as well as excessive moisture. Another common source of leaks was pinholes in condenser coils caused by corrosion and pitting from acidic lint and dirt buildup.

The second most frequent cause of spills was discharges because of operator error. This category of spills accounted for 21% of all reported spills and commonly included boilovers of solvent/distillation from overfilling or excessive operating temperatures, failing to properly close doors, open valves, loose cartridge filter housing, and water separator overflows due to plugging of air vents or fluid outlets.

The next common source of spills responsible for 15% of discharges was leaks

from solvent transfer and storage. 85% of the spills in this category were due to solvent transfer either from overfilling of solvent storage tanks or filling of the equipment. Until the advent of closed loop systems, solvent was delivered either by tanker trucks that pumped solvent directly into ASTs/USTs or by drums. During delivery, solvent could leak from overfilling, leaking hoses especially when the hose is reeled back into the truck. Solvent could also have been discharged when it was transferred from the storage container to the dry cleaning equipment. Sometimes, operators pump hand solvent by hand from the drums or tanks into buckets that are carried to and poured into the machine door or button trap lid at the rear of the machine.

The final type of common spills comprising 13.8% of discharges was spills associated with equipment maintenance. The most frequent kind of spill in this category occurred during filter changes. The filters can contain as much as a gallon of PCE and it was common in the past to store spent cartridges outside the service door where PCE would slowly drain from the used cartridges onto the ground or pavement. The study recommended that filters should be allowed to drain overnight before changing. Solvent discharges can also occur if gaskets or felt washers are not properly seated between filters or if improperly-sized gaskets are used. Another common source of discharges in this category was spills of still bottoms or cooked powder residues during cleanouts of distillation units. The study reported that still bottoms could contain as much as 75% PCE by weight while cooked powder residues could have as much as 56% of PCE by weight. The final common type of spill in this category occurred during servicing of the solvent pump.

The largest average spills were associated with solvent transfer and storage. The area most frequently contaminated was the soil beneath the equipment because of spills associated with equipment operation and maintenance as well as overfilling. The second most common contaminated area was near the service door where solvent transfers frequently occur and undrained filters are stored.

Commentary: The findings of this study can be used to identify areas where samples should be taken during a Phase II environmental site assessment. Samples should be collected from the front and back of the machine. If dry cleaner equipment has been removed, the consultant should look for evidence of the machine such as lag bolts or concrete patches in the floor slab where the bolts had been removed. Coffee-colored stains on the slab may be evidence boilovers, still bottoms or powder residue spills. Samples should also be collected where cracks or expansion joints are located since these can act as pathways to the ground.

Soil samples should also be collected near the solvent storage/transfer areas, around the service door, along sanitary sewer lines and the junction of the sewer line and the sewer lateral, septic tanks and drain fields, and floor drains.

New CEO Certification Requirements Affecting Environmental Disclosure

Back in June, the Securities and Exchange Commission ("SEC") issued an order requiring CEOs and CFOs of companies with revenues during their last fiscal year of greater than $1.2 billion to personally certify under oath that financial statements and reports are materially truthful and complete or explain why such a statement would be incorrect. Because of this certification requirement, some companies are now performing more extensive environmental audits. These companies are conducting more comprehensive environmental assessments because the CEOs want to make sure that financial statements are not understating the impact that environmental liabilities may have on company operations. For example, in the past some companies may have estimated closure costs based on assumptions of the extent of soil contamination beneath lagoons and other waste management units. Now, some companies have retaining environmental consultants to conduct extensive soil and groundwater sampling or environmental compliance audits so that the remediation or environmental compliance estimates in financial statements are based on actual data.

Commentary: In August, 25 charitable foundations petitioned the SEC to issue a new rule mandating environmental disclosure for public companies in accordance with two ASTM standards that

were issued in 2001 for disclosing environmental liabilities and estimating environmental liabilities (see our September 2001 issue). The foundations pointed to the 1998 EPA study that 74% of public companies failed to adequately disclose environmental-liabilities in their 10-Ks. EPA had also pointed out that 16% of filers had not disclosed court-ordered SEPs and just 4% disclosed RCRA corrective actions (see our March 2001 issue).

The foundations said one of the biggest loopholes in the existing regulations was not requiring companies to aggregate all environmental liabilities when determining if the liabilities exceed the materiality threshold for disclosure. Executives of seven socially responsible investment funds with $13 billion in assets also wrote a joint letter to the SEC urging the commission to focus attention on environmental disclosure.

Study Finds High Levels of Arsenic Contamination from Treated Wood

Virtually all of the lumber sold for outdoor uses in the United States is pressure-treated with a chromated copper arsenic ("CCA") to protect the wood from dry rot, fungi, molds, termites, and other pests. CCA contains 22% pure arsenic. A single 12-foot length contains about 27 grams of arsenic, enough arsenic to kill 250 adults Studies have shown that arsenic can leach from treated wood into soil though the rate of leaching can be influenced by a number of factors including climate and the acidity of the soil. A recent study conducted in 45 states has found that treated wood may leach at might higher rates than previously expected and that arsenic is as likely to migrate from old wood products as new wood structures. The study found hot spots of arsenic as high as 250 part per million ("ppm") in soil collected from near or under the structures. These concentrations were on average 20 times the Arsenic cleanup standard for Superfund sites. One quarter of the samples were at least three times the regulatory limit established for drinking water. Previous studies had indicated that a 40-pound child who plays daily on arsenic-treated wood could be exposed to more than five times the arsenic allowed under EPA's proposed drinking water standard.

Commentary: Back in February, EPA announced that it had reached an agreement with the wood-treating industry to phase out the use of CCA in pressure-treated wood and cease using the arsenic-based pesticide by January 2004. Under the agreement, wood manufacturers were to reduce production of CCA products for residential uses by 25% in 2002 and up to 70% in 2003.

In the meantime, EPA recommends that children playing around CCA-treated play structures should wash their hands prior to eating. In addition, the agency recommends that food should not be placed directly on any treated wood. Homeowners are also advised not to burn, saw or sand CCA-treated wood. If a homeowner is going to engage in such activity, they should wear a dust mask, goggle and gloves. Sawdust, wood scraps or remnants of CCA-treated wood should not be used as compost or mulch. Instead, debris should be thoroughly cleaned up and disposed in the municipal solid waste. Likewise, those working with the wood should thoroughly wash all exposed areas of their bodies thoroughly with soap and water before eating, drinking or using tobacco products. Work clothes should be washed separately from other household clothing before wearing them again.

Recently, Florida health officials closed playgrounds that have CCA-treated lumber equipment, removed soil, and disassembled playground equipment built with CCA treated lumber. Florida is recommending that all CCA-treated wood surfaces be sealed at least every two years with a quality, oil-based sealant to create a barrier to arsenic moving to the surface of the wood and reduce the amount of leaching.

EPA Fines Home Builder for EPCRA Violations

Oakwood Homes Corporation of Greensboro, North Carolina agreed to pay a civil penalty of $189,110 to resolve allegations that it failed submit Toxic Release Inventory ("TRI") forms under the Emergency Planning and Community Right-to-Know Act ("EPCRA").

EPA alleged that Oakwood had failed to submit TRIs for propane stored and used at a number of plants for reporting years1996 and 1997. The complaint also alleged that Oakwood failed to file TRI forms for disocyanates for TRI reporting years 1997, 1998 and 1999.

Commentary: The presence of propane can may not only trigger reporting obligations under EPCRA but also require owners or operators of facilities such as warehouses to also prepare Risk Management Plans.

ENVIRONMENTAL INSURANCE

Insurers Tighten Language Of Secured Creditor Policies

In past issues, we have discussed the evolving market for secured creditor policies. Since the summer of 2001, underwriting has tightened considerably and the policies have become more expensive. Exacerbating this trend has been the tendency of "B-Piece" buyers in CMBS transaction to demand stand-alone policies for loans over $3.5 million. Single site policies are not cost-effective though some insurers are working with lenders with high volume single site policies to develop more affordable pricing. At least one insurer has stopped writing secured creditor policies for convenience stores because of large losses suffered on these kinds of loans.

In addition to these market developments, insurers are making changes to their policies. Loan balance policies typically have a double trigger requiring a default and a pollution condition. During the heyday of these policies, liberal underwriting effectively eliminated the pollution condition trigger since some insurers were issuing policies for loans with known environmental conditions. The policy changes are intended to preserve the double trigger.

For example, in the past, a technical default was sufficient to satisfy this default trigger. Many policies now have a modified default definition that only applies to monetary defaults. Likewise, pollution condition has also been changed. In the past, the presence of contaminants above state cleanup levels was sufficient to satisfy this trigger. Now, many policies provide that the insured must be ordered or required to perform a cleanup.

Insurers Eliminating Mold Coverage

Last year, the insurance industry paid $1.3 billion in mold related claims. As a result, insurance companies are now eliminating mold coverage in their homeowner policies.

State Farm Mutual Association, the nation's largest home insurer, has stopped writing homeowners policies with mold coverage in 33 states. Chubb has excluded coverage in approximately 30 states with AIG and Hatford Financial Services in the process of dropping coverage in dozens of states. The second largest home insurer, Allstate, has clarified policy language to eliminate coverage unless the mold is caused by a covered event, such as a storm

Some insurers are making mold coverage available for homeowner policies but have imposed caps usually ranging from $5,000 to $10,000.However, not all states are approving the changes. For example, Louisiana recently refused to approve Allstate's request to cap mold claims to $10,000.

Commentary: Since 1986, most Comprehensive General Liability ("CGL") policies purchased by businesses, landowners, and contractors have included an "absolute pollution" exclusion that bars coverage for liability arising from dispersal of pollutants, irritants or contaminants. Insurers typically argue that mold is an irritant or contaminant covered by this exclusion while insured's argue that mold organisms growing in moist conditions are not pollutants. Even if mold is not considered to be a pollutant, there is also controversy whether mold falls within the "dispersal" language.

Plaintiffs have been using a variety of creative arguments to get around the mold exclusion in homeowners policies. For example, some plaintiffs have argued that mold is an "ensuing loss" that is covered so long as the underlying event such as a burst pipe or leaky roof is a "covered peril" under the policy. Plaintiffs have also argued for coverage under the "efficient proximate cause" doctrine, taking the position that if a covered loss is a proximate cause of the damage, then the resulting mold problem also should be covered.

Insurance companies are also inserting mold exclusions in Environmental Impairment Liability ("EIL") policies. It is possible to have limited mold coverage added back through an endorsement. The coverage conditions will usually include an additional premium, higher deductibles, sublimits for the mold, and a copay usually

around 10%. Insurers will usually perform additional underwriting before adding the mold coverage. This may include evaluation of the type of property, nature of current and prior operations, and review of repair and maintenance records. The endorsement may contain an exclusion for failing to maintain the premises or for construction defects. The definition of bodily injury in the policy excludes emotional distress for mold claims. For bodily injury coverage to apply for mold exposure, there would have to be some manifestation of physical injury.

Pennsylvania State Court Rules LBP Not Covered by Absolute Pollution Exclusion

A Pennsylvania state court recently ruled that the absolute pollution exclusion clause does not bar claims relating to the ingestion of lead- based paint ("LBP"). In *Mistick Inc. and Northside Associates v. Northwestern National Casualty Co.* (Pa. Super. Ct., W. Div., No. 1147 WDA 2000, 8/14/02) a tenant's son suffered lead poisoning from ingesting LBP and sued its landlord who, in turn, sought coverage under its business liability policy. The insurer sought declaratory judgment on the grounds the LBP was a pollutant and that the tenant's son injuries were due to the dispersal of the pollutant.

The court initially found for the insurance company. After the decision, though, the state Supreme Court issued its ruling on *Lititz Mutual Insurance Co. v. Steely (*785 A.2d. 975 (Pa. 2001). In that case, Court acknowledged that LBP was unambiguously a "pollutant" but that the gradual process of how LBP degrades could not be characterized as "discharge, dispersal, release or escape" Applying commonly understood meanings for each of the modes of dissemination described in the insurance policy, the Court reasoned that ordinary meaning of discharge ("a flowing or issuing out"), a release ("the act or an instance of liberating or freeing"), or an escape ("an act or instance of escaping") could not be applied the continual, imperceptible, and inevitable deterioration of LBP. The Court also said that although the cracking and chipping of LBP could be characterized as "dispersal" within the meaning of the exclusionary clause, the term "dispersal" was itself ambiguous and rendered the clause internally inconsistent. Consequently, the Court ruled it was required to resolve the ambiguity in favor of the insured and determined that the exclusionary clause did not preclude coverage of claims arising from ingestion of lead-based paint.

The plaintiff in the Mastic case then appealed to the state Supreme Court who remanded the case back to the Superior Court for reconsideration in accordance with the *Lititz* decision. The insurer tried to distinguish its policy from the one interpreted in *Lititz* arguing that the "dispersal" phrase in its policy had two additional modes of dissemination ("seepage" and "migration") that contemplated the process of cracking and chipping.

However, the Superior Court noted that the state Supreme Court had defined "seepage" as '" the process of seeping,' that is, 'flowing or passing slowly through fine pores or small openings.'" The Superior Court reasoned that since "seepage" contemplated the movement of fluid substances, it could not apply to dried LBP that flaked or chipped

The insurer also argued that the term "migration" when coupled with the provision's broad time reference ("at any time") contemplated the gradual movement described by the Supreme Court. Again, the Superior Court disagreed. The court said that while "migration" was sufficiently broad to encompass gradual chipping of LBP from the wall of a home, it was a vague and general term inconsistent with the other terms used in the exclusion. The court said the provision's additional language, "at any time" did not resolve this ambiguity because it describes the point in time at which movement occurs and did expand or vary the quality of the described movement. Thus, "migration ...at any time" was no more gradual than "migration" unmodified. As a result, the court said the exclusionary language did not clearly include or exclude the physical process of LBP deterioration. Since the ambiguity had to be resolved in favor of the insured, the court concluded that landlord's claim for defense and indemnity was not precluded by the pollution exclusion and the insurer was bound obligation to defend and indemnify the plaintiff.

Voluntary Cleanup Not Covered By CGL Policy

An Illinois appeals court ruled in

Northern Illinois Gas Company v. The Home Insurance Company (2002 Ill. App. LEXIS 784, September 3, 2002) that an insurance company was not obligated to reimburse a policyholder for cleanup costs incurred a state voluntary cleanup program.

In this case, the plaintiff purchased a series of comprehensive general liability ("CGL") policies from a variety of insurance companies between 1955 to 1985. In 1987, the Illinois Environmental Protection Agency ("IEPA") suggested to utility companies that they might want to investigate potential environmental problems at former manufactured gas plants ("MGPs") under their control. The IEPA recommended that the work could be done under the state voluntary cleanup program ("VCP") but indicated that the utilities were not legally obligated to enroll a site in the VCP.

Beginning in 1992, the plaintiff enrolled six sites into the VCP. In 1995, the plaintiff filed a declaratory judgment action against its insurers, arguing they were legally obligated to pay the costs of responding to the contamination by reason of liability imposed by law or alternatively based upon its VCP agreements with the IEPA. The defendants moved for summary judgment on the ground that the plaintiff was not legally obligated to pay for the investigation and remediation of the MGP sites. The trial court granted the summary judgment motions of these insurers.

The appeals court affirmed the lower court ruling. The court noted that the IEPA unequivocally testified that plaintiff had no legal obligation to perform the MGP cleanups. In contrast, the court noted that the cases relied on by the plaintiff had involved tacit threats of state action. In addition, the court found there was authority from Illinois supporting the conclusion that the duty to indemnify is limited to a judgment entered by a court of law.

AIR POLLUTION DEVELOPMENTS

California Companies Fined for Emission Trading Violations

An emissions credit broker was issued a notice a violation by the South Coast Air Quality Management District ("SCAQMD") for filing false trading report under the Regional Clean Air Incentives Market ("RECLAIM") cap and trade program. It is believed that the Automated Credit Exchange ("ACE") engaged in trades for emissions credits that did not exist. ACE faces a maximum civil penalty of $10,000 for each violation.

SCAQMD launched an investigation into ACE's trades after receiving complaints from a number of ACE clients who claimed they paid ACE for RECLAIM trading credits that they never received. Earlier this year, Calpine Corp. filed a lawsuit against ACE to recover millions of dollars in Nitrogen Oxide ("NOx") credits. The parties settled the action and according to a recent SEC filing, Calpine said it received $7 million as a partial recovery of its claim.

Meanwhile, two environmental organizations filed a lawsuit against nine companies, charging that the defendants had failed to obtain sufficient NOx RECLAIM emissions credits. Seven of the defendants have settled the lawsuits in exchange for permanently retiring 200,000 pounds of NOx credits and installing additional pollution control equipment. The credits must be retired during specific compliance cycles in 2002 and 2003. The value of the settlement will depend on the price of the credits when they are retired. During the past year, NOX credits have varied from 65 cents a pound to $2.65 a pound.

The lawsuits had focused on the emissions credits that the defendants claimed from purchasing low-emission vehicles or scrapping older vehicles. SCAQMD had approved a rule allowing mobile source reduction credits in the RECLAIM program but EPA never approved that rule.

NJ Seeks Approval to End Emissions Trading Program

In our March 2001 issue, we reported that the Public Employees for Environmental Responsibility ("PEER") charged the New Jersey Department of Environmental Protection ("NJDEP") was not doing enough to verify that the accuracy of the emissions reductions for its emissions trading program. Recently, NJDEP Commissioner Bradley Campbell requested permission from EPA to scrap the state's Open Market Emissions Trading Program

("OMET").

The OMET was designed to allow air emission sources to comply with emissions limitations for volatile organic compounds ("VOCs") and NOx by trading emissions credits. Each credit is equal to 100 tons of VOC or NOX emissions. EPA conditionally approved the state implementation program ("SIP") in June 2000 provided NJDEP corrected some deficiencies in the OMET program. NJDEP did not correct the flaws and Commissioner Campbell concluded that the problems with the OMET program went beyond the issues identified by EPA. Campbell indicated that the program did not have sufficient mechanisms to verify emissions reductions and that credits were issued for emissions reductions that had been occurred before the OMET program went into effect. In addition, the company retained to operate the OMET's online registry of emissions transactions and program hotline shut down the registry and hotline in September 2001. A subsequent investigation by the DOJ has raised questions whether the company adequately verified emissions reductions. Campbell also indicated that there was evidence that some facilities had developed compliance strategies based completely on their ability to purchase emissions credits in the future even though there was no assurance that such credits might be available.

Earlier in the year, EPA had indicated that facilities using emissions credits to comply with emissions limitations could be subject to federal enforcement because the agency had not yet approved the SIP. To protect facilities that had used the OMET in good faith, Campbell asked EPA to issue limited approval of the SIP revisions. NJDEP will terminate the OMET through formal rulemaking.

Commentary: In the wake of the recent accounting irregularities, we anticipate that the states and EPA may begin to scrutinize emissions programs more closely to verify that facilities have actually achieved emissions reductions for the emissions credits that they have registered.

Utilities Urged to Bank SO2 Emission Credits

In our May issue, we discussed that 29% of the Sulfur Dioxide ("SO2") allowances issued under Phase I of the Acid Rain SO2 Cap and Trade program were not used. According to a study recently issued by ICF Consulting of Fairfax, Virginia, utilities and other major industrial sources of SO2 emissions should bank these allowances because the allowances will grow more valuable under Phase II of the Acid Rain program.

Currently, there is an excess of approximately 9 million SO2 allowances available for sale. One of the principal reasons for the glut is that regulated sources were selling allowances to raise cash flow and improve earnings. However, ICF predicts the excess inventory will disappear by 2008 and prices will rise dramatically.

As we explained in our May issue, the demand for SO2 credits is expected to rise as Phase II is implemented. When Phase II began earlier this year, 2,000 combustion units became subject to the Acid Rain program. These additional sources will need to acquire SO2 allowances. Moreover, the total allowable SO2 emissions under Phase II will be capped in 2010 at 8.5 million tons representing a 50% reduction from 1980. In addition, EPA may impose further SO2 emission reductions as part of its new PM 2.5 fine particulate standard that will go into effect in 2005.

If regulated sources do not obtain SO2 allowances, they will have to install expensive scrubbers or other pollution control equipment which could increase the marginal cost of pollution controls and increase demand for allowances. The average price for 2002 allowances in the spot market is $167.74 per allowance while the average price for 2009 allowances is $81.87.

Commentary: The Acid Rain Program established an annual national cap on SO2 emissions. Each year, EPA issues allowances to existing sources to match that cap. An allowance gives affected sources the right to emit one ton of SO2 per year. A plant's total annual emissions cannot exceed its allowances. Allowances are transferable, allowing market forces to determine their price. If a source reduces its SO2 emissions more than required, it can sell the excess allowances or bank the allowances for future use. However, the CAA mandates that a limited number of those allowances are withheld and auctioned. The auctions help ensure that new electric generating plants

have a source of allowances beyond those initially allocated to existing units. Proceeds from the auctions are returned to sources in proportion to the allowances withheld. In addition to allowances offered by EPA, private parties may offer allowances for sale in the auction. Allowance auctions are held for the current year and seven years in advance to help provide stability in planning for capital investment. According to EPA, SO2 emissions are 5 million tons below 1990 levels and acid deposition in the eastern United States has declined by as much as 30%.

More Guilty Pleas In New York Asbestos Case

Four men pleaded guilty to criminal violations of the asbestos rules in connection with asbestos abatement projects in upstate New York. The General Manager of AAR Contractor Inc. faces a maximum sentence of 77 years in prison and/or possible maximum fines of $3.5 million, plus restitution to victims. He admitted to failing to comply with asbestos notification requirements and intentionally contaminating buildings with asbestos to defraud owners. He also admitted to intentionally leaving asbestos-containing materials ('ACM") in buildings and providing false laboratory reports indicating that asbestos had been removed. A second man faces a possible maximum sentence of 15 years in prison and/or up to $1 million in fines plus restitution. The other two individuals face maximum sentences of up to 10 years in prison and/or $500,000 fines.

USA Remediation, Comprehensive Employee Management, Inc. and four supervisors were indicted in connection with an asbestos removal project for the Buffalo-Niagara airport. The indictment alleges that the companies improperly removed 25,000 linear feet of ACM from a former Westinghouse plant in 1999 in connection with an airport expansion project. The defendants were charged with failing to comply with asbestos work practices, making material false statements to the Federal Aviation Administration and falsifying documents. The two firms face potential fines of up to $500,000 for each count while the individuals may be subject to fines of up to $250,000 and five years in prison for each count.

The owner of Hilton Management was indicted for numerous violations of the asbestos regulations. The indictment charged that the defendant failed to provide the required notification, did not use a licensed asbestos abatement contractor, failed to comply with asbestos workpractices and improperly disposing the ACM. In addition, the defendant was charged with failing to comply with the CERCLA reporting requirement by notifying the National Response Center of the release of asbestos fibers into the air. Each CAA violation carries a maximum penalty of $250,000 and five years in jail. The maximum penalty for the CERCLA violation is a fine of $250,000 and prison term of three years.

Building Owners Fined for Improper Asbestos Removal

EPA filed an administrative complaint seeking a $54,200 penalty from CVS Corp. in connection with the demolition of a building in Reynoldsburg, Ohio. CVS bought the site to build a drugstore and failed to comply with the asbestos regulations during the demolition. EPA alleged the company failed to file the required notice, did not comply with the asbestos workpractices and improperly disposed ACM-contaminated debris.

The owner of the Old Zumbrota Fire Station in Zumbrota, Minnesota was fined $35,000 for improperly removing asbestos in 1999. The state Pollution Control Agency found 12 bags of ACM and damaged pipe insulation during an inspection in June 2000. The state agency determined that the owner failed to comply with the asbestos notification requirements and had hired an unlicensed contractor to remove the ACM. As part of the settlement, the owner will complete an ACM asbestos survey and properly dispose the ACM.

Building Owners Indicted for Criminal Violations of Asbestos Rules

Three individuals were indicted for improperly removing ACM from a commercial building in Martinsburg, Virginia. The indictment alleges that the three individuals purchased a commercial building in October 2000. Before beginning a renovation project, the defendants retained a consultant who determined that the building had asbestos floor tile on two floors and that it would cost $20,000 to remove and dispose of the floor tile. Instead of retaining a

licensed asbestos abatement contractor, the building owners hired untrained workers to remove and dispose the tile at an illegal disposal site in Martinsburg. The six count indictment charged that the three building owners failed to provide the required advance notice of the renovation work, failed to comply with asbestos workpractices, and failed to have a licensed supervisor oversee the renovation If convicted, the defendants face maximum fines of $250,000 for each violation and up to five years in prison.

Companies Will be Required to Perform Indoor Air Monitoring at Former Facilities

EPA will require 10 Silicon Valley high-tech companies that once operated manufacturing plants in Mountain View, California to conduct air monitoring inside several offices. Groundwater beneath the buildings has been contaminated with trichloroethylene ("TCE") from the prior operations. The agency is concerned that TCE vapors are seeping into the office buildings through cracks in the foundation and the soil. The buildings are now occupied by AOL Netscape, Nokia and Veritas Software. EPA will require a number of semiconductor manufacturers including Intel and Fairchild Semiconductor to submit a work plan by December 1st. The companies will have to collect soil gas, indoor air and outside air sampling.

Commentary: In our March issue, we discussed studies suggesting that EPA and state environmental agencies were relying on a computer model to predict indoor air concentrations that may underestimate the actual levels of contaminants in the indoor air. When a building is located on lad above an aquifer that is contaminated with VOCs, a purchaser should determine if any investigation was done to determine if contaminants are seeping into the indoor air.

WATER POLLUTION/ENDANGERED SPECIES

Federal Court Rejects Takings Claim for Wetlands

The Court of Appeals for the Federal Circuit ruled that property owners did not suffer a regulatory taking when they were only allowed to develop a portion of their property because of the presence of wetlands. In *Walcek v. United States* (Fed. Cir., No. 01-5108, 9/11/02), the plaintiffs purchased a 14.5-acre parcel of land in 1971 shortly before the passage of the Clean Water Act ("CWA") in 1972. The plaintiffs hoped to develop the land to supplement their retirement income.

At the time of the transaction, approximately 5 acres of the property was identified as wetlands by the state of Delaware and the parties stipulated at trial that there was no reasonable likelihood that the state would have allow residential development on the mapped wetlands. In addition, a portion of the parcel was below the mean high water mark and was subject to federal regulation under section 10 of the Rivers and Harbors Act of 1899 prohibiting construction that impacted navigable waters without approval by the Army Corps of Engineers ("Corps"). Beginning in 1968, the Corps had exercised public interest reviews that included environmental and conservation concerns in addition to purely navigational impacts.

In 1972, 13.2 acres of the property became regulated as jurisdictional wetlands under section 404 of the CWA. The plaintiffs did not realize the property contained federally regulated wetlands until 1984 when they agreed to sell the land for $1 million. The sale was contingent upon the purchaser obtaining all necessary permits for the construction and sale of 60 or more townhouse units.

After the sale fell through, the plaintiffs tried to have the property zoned for commercial development. When this was unsuccessful, the plaintiffs decided to pursue a border-to-border, 77-lot residential

development of the property and began filling the wetlands. When the Corps became aware of these activities, it issued a cease and desist order.

Beginning in 1988, the plaintiffs filed a series of wetlands applications. The Corps initially denied the permit application in 1993. The plaintiffs initially filed a temporary takings claim because of the seven-year delay in processing the wetlands application. However, the Court of Federal Claims ruled that the permit denial did not constitute a taking as a matter of law and that any delay was due to the "plaintiffs' own failure to complete the permitting process as well as their strategic decision to initiate the lawsuit rather than pursuing the permitting process to a final merits determination. The case was dismissed without prejudice.

In 1996, the Corps issued a permit that allowed the plaintiffs to develop 2.2 acres but required them to create 4.4 acres of wetlands as mitigation measures. Although the permit would have allowed the construction of 28 homes, the plaintiffs brought a takings claim for the entire parcel. The Court of Federal Claims ruled that the 1996 permit did not create a categorical taking because it allowed development of 2.2 acres of the wetlands and therefore did not deny "all economically beneficial or productive use of land". The court also held that 1996 permit merely caused a non-compensable diminution in value that allowed the plaintiffs to realize their reasonable expectations in the development of the property.

On appeal, the Court of Appeals for the Federal Circuit ruled the because the plaintiffs had failed to argue that the 11 acres of wetlands on which development was barred constituted the relevant parcel, the court would not consider that argument on appeal. The court then determined that the Court of Federal Claims had properly determined that the plaintiffs were not totally deprived of all economically viable use of their land, and affirmed the conclusion that no categorical taking had occurred.

EPA Wetlands Enforcement Actions

Tammany Holding Corporation of Slidell, La. pleaded guilty and fined $300,000 for dredging and discharging material into a local lake without a permit while building a residential development. The company also agreed to pay $38,000 in restitution to four environmental groups.

EPA is seeking a $55,000 penalty from the owner of Agee Construction Company for knowingly discharging dirt and rock into a river to construct bank stabilization and riprap projects at several waterfront homes without obtaining a wetlands permit.

A California developer was fined $1 million for destroying artificial wetlands that provided habitat for frogs on the endangered species list. The owner of West Coast Homebuilders Inc. pleaded guilty to ordering employees to drain two ponds that he knew contained breeding populations of threatened frog species. As part of the settlement, the developer agreed to pay $300,000 in criminal penalties, a $300,000 civil penalty, $300,000 in restitution, $75,000 to the state Fish and Game Preservation Fund and $25,000 to county hazardous material training and resources trust fund. In addition, the developer agreed to preserve a 640-acre parcel to provide substitute habitat for the frog. Finally, the company was placed on three years probation.

POTW May Sue Discharger Under State Law

A regional sewage authority was allowed to bring an action against a customer of the treatment plant for excessive discharges under a state clean water act even though the defendant did not discharge pollutants into waters of the state. In *Chalfont-New Britain Township Joint Sewage Authority v. Bucks Co. Water & Sewer Authority* (168 MAP 2001), the plaintiff allocated a portion of its treatment capacity to other sewage authorities that did not have their own treatment plants. The defendant's discharges exceeded its allocation and prevented the treatment plant from meeting its permit limitations.

The plaintiff then sued the defendant, arguing that its excessive discharges violated the Pennsylvania Clean Streams Law that prohibits discharges of pollutants into state waterways without a permit. The defendant argued it could not be liable because it did not directly discharge any pollutants into any waterways and that it was the plaintiff that had violated the law by violating the terms of its permits. A trial court agreed but an appeals court ruled that the law specifically applied to indirect dischargers whose discharge results in

pollution by disrupting the POTW treatment process.

Commentary: Many businesses discharge wastewater into local sewer systems. Purchasers of businesses that are likely to generate wastewater with hazardous substances or otherwise affect the treatment process of the local sewerage plant should make sure that these issues are addressed during the due diligence period. The local sewer authority should be contacted to determine if the business is required to obtain a permit and if it is in compliance with any discharge permit or authorization. The compliance of the treatment plant should also be checked. If a sewer plant is unable to meet the conditions of its permit, it may impose pretreatment requirements on its commercial customers or impose surcharges based on the volume of wastewater discharged into the system. For large commercial businesses, these surcharges can be significant.

Golf Courses Can Serve as Mitigation Banks

Golf courses have been a popular end use for brownfield sites. According to a Purdue University study, golf course may also be able to serve as mitigation banks because constructed wetlands on golf courses can improve water quality.

The five-year study used three wetland ponds incorporated into a renovated golf course. The researchers determined the constructed wetlands could improve water quality by reducing or breaking down a variety of pesticides and chemicals that are commonly used at golf courses. They found that the golf course grass also trapped nutrients and chemicals contained in runoff from adjacent areas. As a result, the constructed wetlands not only cleaned runoff only from the golf course but also two residential highways, a motel parking lot, a gas station and 200 homes.

The researchers said that most golf course wetlands are designed for aesthetics purposes. However, minor changes in the ponds can optimize their usefulness as runoff filters. For example, varying the speed and depth of water can enhance the growth of different populations of microbes that will improve the efficiency of the constructed wetlands.

EPA Awards Wetlands Enhancement Grants

The Williams/Transco Gas Company was recently awarded $7,500 for a wetlands enhancement project in Chester County, Pennsylvania. The award is part of the Five-Star Restoration Grant Program, providing community-based partnerships grants to support wetlands and streamside restoration projects

Williams/Transco enhanced a quarter acre wooded wetland by creating a 120-foot berm. The berm contains water during wet times of the year, provides habitat for various species of wildlife and allows rain and snow melt to return to the ground, as opposed to running across surrounding agricultural fields and roads. The funds will be used to purchase native plants for the wetland restoration project.

Commentary: The Five-Star Restoration Project grants are awarded on a competitive basis. Grants are based on the program's educational and training opportunities for students and at-risk youth, the ecological benefits to be derived, and the project's other cultural and economic benefits to the community.

EPA Stormwater Enforcement Actions

Stokes Automotive Parts, Inc. of Jefferson, Maryland agreed to pay a $5,000 penalty to resolve allegations that it allowed contaminated stormwater to discharge into a local creek without obtaining a stormwater permit. Under the agreement, the auto salvage yard obtained a stormwater permit and will implement required storm water pollution controls.

EPA also cited seven related companies in northeastern Pennsylvania for a variety of stormwater violations. All of the facilities are primarily engaged in cutting, shaping, and finishing bluestone used for construction and landscaping. The stone-cutting operations use substantial amounts of water to suppress dust and cool stone-cutting equipment and can produce significant runoff if the water is not controlled. The facilities include Powers Stone, Inc.; B.S. Quarries, Inc.; Premier Bluestone, Inc.; Norton Stone Company; Glenwood Stone Company, Inc.; Herb Kilmer & Sons, Inc.; and Meshoppen Stone, Inc. In addition, EPA is seeking $110,000 in penalties from Powers Stone, Inc. for the failing to obtain a permit and failing to

implement an erosion and sediment control plan.

Commentary: Storm water runoff from industrial and construction sites often contains pollutants such as oil and grease, chemicals, nutrients, and oxygen-demanding compounds. Storm water permits require preparation of a storm water pollution prevention plan that can include a variety of management practices such as housekeeping, spill prevention, storage of properly contained waste fluids sheltered from rainfall, and employee training.

HAZARDOUS WASTES/USTS

EPA Issues Hazardous Waste Delisting Report

According to an EPA report, 136 waste streams at 115 different facilities have been exempted from the Resource Conservation and Recovery Act ("RCRA") in the first 20 years of the program. Because these so-called "delisted wastes" are not subject to RCRA's hazardous waste management requirements, EPA estimated that the delist program has saved businesses at least $105 million annually with 85% of those savings realized by facilities in the form of reduced treatment and disposal costs. The agency estimated that the 20 year net cost savings to society was between $1.2 billion to $2.4 billion.

45 million tons of the delisted waste wastewater which accounted for 80% of the volume of delisted waste steams. The largest category of delisted wastes was electroplating wastes (F006, F009 and F0019), accounting for 51% of the waste stream exemptions. Solvent wastes (F001-F005) were the next largest category of delisted waste with 15% of the granted petitions.

EPA did not estimate the environmental benefits of the delisting program but said it had no evidence that there were any releases associated with the delisted wastes or little reason to believe the delisted wastes were impacting the environment. The states with the most exemptions were Ohio, New York, Tennessee, Indiana, Pennsylvania, Alabama and Arkansas.

EPA Considering Extending RCRA Financial Assurance Requirements

In our September 2001 issue, we discussed the findings of an audit report by the EPA Office of Inspector General that concluded that many RCRA-regulated facilities have not established adequate financial assurance mechanisms to cover the closure and post-closure costs of those facilities. The report found that 19% of the facilities did not have any financial assurances.

At the urging of state environmental officials, EPA is now considering extending the financial assurance requirements to hazardous waste recycling facilities. State regulators have indicated that the recycling facilities are low-profit operations that experience high turnover and frequently go out of a business, leaving behind hundreds of contaminated sites. State officials also complain that many facilities particularly auto and oil recycling operations are engaging in sham recycling where they collect waste fees with no intention to recycle the collected materials.

Commentary: Another area that EPA has been urged to review is the net worth test that many facilities used to satisfy the financial assurance requirements. To meet the net worth test, a facility owner or operator must have a net worth at least $10 million more than the estimated closure and post-closure costs. EPA chose this level because studies found that firms with less than $10 million in tangible net worth were four times as likely to file for bankruptcy. The OIG audit report found that facilities using the net worth test often fail to meet the test in subsequent years and that it was not a good predictor of long-term solvency. EPA regulations require facilities using this means of financial assurance to file annual updates. The OIG report recommended that EPA and delegated states consider requiring facilities to submit financial information when there is a reasonable belief that the owner or operator not longer meets the net worth test.

As pointed out in our last issue, the closure and post-closure costs are often underestimated. Indeed, the OIG report found that in one EPA region, facilities had

underestimated closure costs by a total of $91 million and post-closure costs by a total of $1.7 million. Moreover, in the wake of the recent accounting scandals there is growing concern about the veracity of company net worth estimates.

EPA is also considering establishing strict ratings for insurance companies used to provide financial assurance. The OIG report had criticized the use of "captive" insurance companies as well as "fronting" arrangements where the insured is required to reimburse the carrier for any claims paid for closure and post-closure costs.

The OIG report had also indicated that state regulators had problems determining if the insurance policies complied with the RCRA requirements. Because of the lack of a standardized insurance policy for financial assurance, OIG found that states often had to create special legal teams to review policy terms and exclusions. OIG said that in some cases that a facility might obtain a policy to demonstrate financial assurance and then cancel the policy without notifying the state. Moreover, insurers often did not notify states when policies were cancelled.

According to the OIG, surety bonds remained the most common form of financial assurance. While facilities may only use surety companies that are on the Treasury Department Circular 570 List, OIG noted that the risk of a surety removed from this list was higher than the risk of failure by companies with a net worth less than $10 million. As a result, the OIG recommended additional controls be implement for surety bonds such as limiting the total amount of bonds that can be issued by a surety company.

OIG also said that states failed to take litigation risks into account when approving surety bonds. OIG noted that surety bonds differ from insurance because that the surety only becomes liable if the facility owner or operator fails to comply with closure or post-closure requirements. OIG indicated that state agencies may have to litigate against the surety and that the time and resources spent pursuing the surety could exacerbate environmental problems at the facility.

Investors Using RCRA 7002 to Profit from Cleanups

Prior issues have discussed how property owners may use the citizen suit provision of RCRA section to force former owners or operators to remediate contaminated property. While the citizen suits may not be brought for wholly past violations of RCRA, federal courts have held that the continuing presence of contaminated groundwater represented a continuing violation of RCRA.

Some real estate developers are now using RCRA 7002 as part of an investment strategy. These investors will buy discounted mortgage notes and then file a RCRA 7002 action seeking to compel either former or adjacent property owners or operators to remediate the site. Once the cleanup is completed, the plaintiff will then either sell the note at a substantial profit or purchase the property and flip the now more valuable property to a developer.

Commentary: Owners of property contaminated with petroleum cannot file contribution or cost recovery actions under CERCLA because petroleum is excluded from the CERCLA definition of hazardous substances. RCRA 7002 addresses a broad universe of contaminants including petroleum. However, plaintiffs are not entitled to cost recovery but only injunctive relief in the form of an order requiring the defendant to remediate a site. On the other hand, parties seeking to compel cleanups under a RCRA citizen suit may also be eligible for reimbursement of their attorneys' fees As a result, RCRA 7002 can be a very important tool for property owners.

To bring a RCRA 7002 action, a plaintiff must establish that the defendant (1) was contributing or have contributed to the handling, storage, treatment, transportation or disposal of solid or hazardous wastes which may present an (2) imminent and substantial endangerment to human health or the environment. To show that there is "imminent" harm, the plaintiff does not have to establish that actual harm will occur immediately but simply allege that there is a risk of threatened harm. Sometimes, the mere presence of contaminants in groundwater is enough to demonstrate there is an "imminent" harm. To establish "substantial endangerment", a plaintiff does

not have to present proof of actual harm or present risk assessments that quantify the risk but simply show a threatened or potential harm.

UST Enforcement Actions

EPA filed a complaint against two individuals and five corporate defendants for failing to comply with the UST regulations at five gas stations in Brooklyn and Queens. The agency charged the defendants qith failing to upgrade USTs to the 1998 UST Performance standards, failing to perform leak detection and procedures and failing to comply with UST temporary and permanent closure requirements. The violations date back to 1992 when EPA investigated over forty facilities allegedly owned by one of the corporate defendants. The company paid a penalty and entered into a consent decree in 1997 where it committed to comply with UST requirements. However, subsequent EPA inspections revealed that the defendants had failed to comply with the terms of that consent agreement at the five facilities. In addition to injunctive relief, EPA is seeking fines for violating the terms of the 1997 consent agreement.

PAM Management, Inc., the owner and operator of the Hickory Run Truck Plaza in White Haven, Pa. agreed to pay a $31,111 penalty to resolve claims that the company failed to perform inventory monitoring for three 10,000-gallon gasoline USTs and two 20,000-gallon diesel USTs. EPA also cited the company for having non-functional leak detection monitors for its three 10,000 gallon gasoline storage tanks. The company has certified that it is now in compliance with UST regulations.

Hi-Noon Petroleum, Inc. (Hi-Noon) agreed to pay a $23,125 penalty and spend $69,375 to purchase new piping for drinking water supply system of Browning, MT's. The settlement resolves allegations that the company failed to monitor and timely respond to a release of gasoline from USTs at its convenience store located at the Blackfoot Reservation. Thus far, approximately 2,180 cubic yards of petroleum-contaminated soil has been removed and about 111,000 gallons of groundwater have been treated. The new pipe will replace and repair leaking or deteriorated pipes in the drinking water system.

EPA filed an administrative order against Norm Poole Oil, Inc. of Ontario, Oregon failing to conduct adequate leak detection at all three facilities, failing to upgrade equipment by the 1998 deadline, and not timely reporting a suspected release of gasoline.

Administrative Costs Consume Smaller Percentage of Federal LUST Trust Fund

During the first half of 2002, state UST programs spent 37% of the nearly $60 million they received from the federal Leaking Underground Storage Tank ("LUST") trust fund on administrative expenses In the first half of 2001, states spent 43% of LUST funds for administrative purposes.

The percentage of LUST Fund appropriates used by states for corrective action increased slightly from 32% in 2001 to 34% in the first half of 2002. States used 29% of their LUST Fund appropriation for enforcement which was an increase over the 25% for the first half of 2001.

Commentary: The federal LUST Trust Fund currently has a balance of $1.7 billion. EPA was authorized to use the LUST Trust Fund to finance corrective action for releases of petroleum under limited circumstances though EPA has used the LUST trust fund primarily to help states finance their UST programs.

The LUST trust fund may not be used until the EPA or designated state official determines that the funds are necessary to protect human health and the environment and one of the following circumstances occurs: the owner or operator is unidentifiable; the required corrective action exceeds the financial resources of the owner and operator including any available financial assurances; the owner or operator is unwilling or unable to comply with a corrective action order; and prompt action is required to protect human health and the environment. Owners or operators of USTs from which releases have occurred are strictly liable for funds dispersed from the LUST Trust Fund.

Legislation has been introduced in Congress (S.1850) that would require that 80% of the LUST Fund be disbursed to the states and that the states be given greater flexibility on how they may use the funds. The legislation would also mandate that $125 million of the LUST Fund be used for

MTBE cleanups each year.

EPA Approves Nebraska UST Program

In our November 2001 issue, we discussed how state UST programs may differ from the federal program. EPA's recent approval of the Nebraska program illustrates this point.

The Nebraska program is broader than the federal program because it regulates UST systems used to store fuel solely for use by emergency power generators, certain USTs used to store heating oil, any tank used for consumptive on-site purposes, requires registration of permanently abandoned systems, allows aboveground storage tanks to be eligible for reimbursement from the state UST cleanup fund, imposes licensing and certification requirements on tank installation and removal contractors, licenses and imposes a remedial action fee on certain refiners and suppliers, and requires any person who deposits regulated substances in a tank to make certain notifications to owners and operators of UST systems, and requires UST systems closed between the December 22, 1988 deadline for upgrading USTs and January 1, 1989 to be closed in accordance with state closure requirements.

However, the Nebraska program is not as broad as the federal program because Nebraska does not regulate tank systems installed between December 22, 1988 and January 1, 1989 as new USTs. For tank systems installed during this 9-day window, EPA retained authority to assume enforcement responsibilities.

Commentary: RCRA authorizes EPA to authorize states to administer their state UST programs in lieu of the federal UST program if EPA determines that the state program is "no less stringent" than the Federal program Many so-called delegated states have UST programs that are more stringent requirements than the federal program. EPA has approved 31 state UST programs. These states are Alabama, Arkansas, Connecticut, Delaware, Georgia, Iowa, Kansas, Louisiana, Maine, Maryland, Massachusetts, Minnesota, Mississippi, Montana, Nevada, New Hampshire, Nebraska, New Mexico, North Carolina, North Dakota, Oklahoma, Rhode Island, South Carolina, South Dakota, Tennessee, Texas, Utah, Vermont, Virginia, Washington, and West Virginia.

UST Operator Denied Reimbursement from State UST Trust Fund

A South Carolina appeals court upheld a denial of claim for reimbursement filed by an operator of a convenience store. In *Worsley Cos. V. South Carolina DHEC* (S.C. App. Ct., No. 3537 7/29/02), the convenience store operator spent approximately $460,000 to remediate a release of gasoline at the leased premises and then paid the property owner $400,000 to settle a lawsuit for property damages. The operator then sought reimbursement from the State Underground Petroleum Environmental Response Bank ("SUPERB") Financial Responsibility Fund. However, the state Department of Health and Environmental Control ("DHEC") denied the claim because the landlord did not fall within the definition of a third party. The DHEC noted that the SUPERB Act expressly excluded claims for reimbursement to the owner of the property where the storage tanks are located.

The operator then appealed, arguing that the owner only had a beneficial interest in the property because it had no right of control over the property and that the prohibition on payments to owners was intended to prevent fraud. However, the court found the statute only distinguished between owners of property where tanks were located and the owners of property without tanks. The court said it gave great deference to the legislative scheme and ruled that the DHEC's interpretation of the statute was rationale.

TOXIC SUBSTANCES

EPA LBP Enforcement Actions

EPA recently filed an administrative complaint against two Chicago apartment building owners seeking $76,890 in civil penalties. The complaint alleges that the building owners failed to comply with the

lead-based paint ("LBP") disclosure rules at 10 apartments they own.

A sandblasing company was fined $24,750 by EPA for improper handling of LBP debris during renovations of a building. During sandblasting of the building, D&D Sandblasting generated large amounts of lead-containing debris. The administrative complaint alleged that D&D failed to adequately test the paint for lead, and failed to appropriately manage the debris as hazardous material. As a result approximately 9 tons of the LBP debris was shipped to a solid waste landfill that is not licensed to accept hazardous waste. Because the waste was improperly handled, lead dust contaminated large parts of the building, including a dance studio for children that employed a pregnant dance director.

SUPERFUND/BROWNFIELDS

EPA Issues Draft Guidelines for New Brownfield Funding Program

Earlier this month, EPA issued its "Proposal Guidelines for Brownfields Assessment, Revolving Loan Fund and Cleanup Grants" to assist applicants for federal brownfield funding. EPA estimates that 200 grant awards will be issued in fiscal year 2003.

The guidelines contain some interesting clarifications on what parties may apply for grants, limitations on how the funds may be used and the sites that are eligible for brownfield funds. For example, EPA has determined that grant recipients must own the site for which they are seeking funding. In addition, universities and other non-profit educational organizations fall within the agency's definition of non-profit organizations.

For the assessment grant program, eligible entities may apply for up to $200,000 for sites contaminated by hazardous substances, pollutants as well as hazardous substances that are mixed with petroleum. In addition, applicants may seek another $200,000 for petroleum-contaminated sites. Applicants may seek a waiver of the $200,000 limit and apply for up to $350,000 for such sites. However, in no event shall an applicant receive more than $400,000 (or $700,000 if waivers are approved). The assessments will have to be completed with two years.

For Revolving Loan Funds ("RLF"), applicants may receive up to $1,000,000 for an initial RLF grant. The funds may be used for sites contaminated with hazardous substances, pollutants, mixed wastes and petroleum. All RLF awards require a 20% cost share in the form of money, labor or services though an RLF grant recipient could apply for a waiver based on hardship. Recipients may use fees, interest on loans, repayments of loan principal and other program income to meet their cost share requirement. At least 60% of the RLF grant must be used to capitalize the RLF. The recipient of the RLF may use the RLF to issue no-interest or low-interest loans. RLF grant recipients may also use up to 40% of the RLF to award cleanup subgrants for sites owned by a subgrantee. The subgrants do not have to be repaid. The RLF-funded cleanups must be completed within five years.

Eligible applicants may also apply for Cleanup Grants of up to $200,000 per owned property with a maximum of five sites per applicant. The cleanup grants also require a 20% cost share and must be completed within two years.

The guidelines also contain information to help applicants determine if a particular site is eligible for brownfield funding. One category of sites that had been excluded from eligibility by the 2002 Brownfield Amendments was sites subject to CERCLA Removal actions. The guidelines indicate that for purposes of the brownfield funding program, a site will be considered subject to a removal action if EPA has issued an action memo, an EA/CA approval memo, has mobilized on-site or issued a notice of federal interest to one or more PRPs. A removal action will be deemed to have completed and a site eligible for brownfield funding when the actions specified in the action memo are met or when the pollution report documents that the contractor has demobilized and left the site. If an assessment grant indicates that a removal action is necessary, the grantee may continue to use the grant to fund

additional assessment activities provided this work is coordinated with the on-scene coordinator.

EPA determined that RCRA facilities that are eligible for funding include interim status TSDFs that are not subject to an administrative or judicial order/consent decree, interim status TSDFs that are subject to administrative or judicial orders that do not include corrective action and parcels of RCRA facilities not covered by a permit or administrative or judicial order. RCRA facilities ineligible for brownfield funding are permitted TSDFs, interim status TSDFs subject to administrative orders requiring corrective action, facilities with judicial or administrative orders/consent decrees requiring corrective action and facilities that have notified EPA or a delegated state that a disposal unit will be closed and have closure requirements specified in a permit or closure plan.

The 2002 CERCLA Amendments also excluded properties subject to the jurisdiction, custody or control of the federal government. The guidelines provide that privately owned Formerly Used Defense Sites ("FUDS") and the Energy Department's Formerly Used Sites Remedial Action Program ("FUSRAP") might be eligible as well as other former federal properties that have been disposed by the federal government.

Sites with a release of PCBs and subject to remediation under TSCA were also ineligible for brownfield funding under the 2002 Amendments. EPA clarified in the guidelines that all portions of properties are eligible for assessment grants except where the agency has initiated an involuntary action against any person to address the PCB contamination. EPA defines an "involuntary action" to include enforcement actions for illegal disposal, TSCA order to characterize or remediate a spill or old disposal, penalty for violating TSCA remediation requirements, CERCLA removal action or RCRA corrective action under §3004(u) or (v). For cleanup grants and RLF grants, all portions of properties are eligible except where EPA has an ongoing action to address PCB contamination.

The 2002 CERCLA Amendments also excluded sites where response actions were financed from the federal LUST Fund. EPA determined in the guidelines that the exclusion applies to sites where LUST money is being used on actual assessment or cleanup. However, EPA indicated the brownfield funding may be available for sites where LUST money has been used by a state for oversight activities and not for specific assessment or cleanup activities at the site, all USTfields pilot sites, sites where LUST-funded assessment activities were completed and the state has determined the parcel is a low-priority UST site, and sites where LUST money was used for emergency activities and the state determines the site is not eligible for any further LUST funding but additional assessment or cleanup is required for economic revitalization of the site. While these sites would be good candidates for brownfield funding, EPA would have to make site-specific determinations that the financial assistance for these sites will achieve the goals of the brownfield program and statutory criteria. These criteria include: protection of human health and the environment, promote economic development, creation or preservation of certain kinds of open space, greenways, recreational property or other property used for non-profit purposes.

EPA has proposed a two-step competitive selection process for all three funding programs. Eligible applicants must submit initial proposals by November 27th. Regional panels will evaluate the proposals on a pass-fail basis for threshold criteria such as applicant eligibility and community notification. Proposals that satisfy the threshold criteria will then be ranked using a numerical scoring system. Proposals may be awarded up to 40 points for community need, 40 Points for leveraging of additional resources, and 20 points for ability to manage grants. For RLFs, applicants may receive up to 40 points for describing the target market for loans and subgrants.

Applicants ranking highest in each region for each fund program will be invited to submit final proposals by March 5, 2003. National Evaluation Panels rank the final proposals as follows: 15 points for sustainable reuse of brownfields/development potential, 20 points for reducing threats to human health and the environment, 15 points for reuse of existing infrastructure, 15 points for creation or preservation of greenspace and open space,

and 20 points for community involvement. RLF applicants will also have to submit a Business Plan. This criterion will be worth up to 20 points.

Commentary: Despite federal and state brownfield programs, the lagging economy is making it difficult sellers to disposing commercial properties with environmental issues. Companies can incur significant carrying costs for these sites. For example, Bayer is incurring $7 million a year for a million square foot complex of assembly lines in Elkhart, Indiana with annual property taxes of $479,000. The property has an estimated value of $12 million and could cost $20 to demolish. Because the property has never changed hands, no environmental assessments have ever been performed. Honeywell is also trying to sell many obsolete properties across the country.

EPA Announces Smart Growth Grants

EPA announced $405,000 in grants to nine communities under its Smart Growth program. Each community will receive $45,000 to incorporate smart growth approaches into brownfield redevelopment projects.

The funds will be used to identify and market brownfields sites that use Smart Growth features, develop site plans that incorporate smart growth elements such as a mix uses and transportation choices, capacity-building for local officials and builders on how to redevelop suburban commercial centers using smart growth techniques, mathematical models to evaluate the impacts of smart growth redevelopment of brownfields, and regional approaches that connect urban Brownfields reuse with suburban and rural open space preservation. In addition to the grants, the initiative provides technical assistance to states and communities to prioritize open space for preservation.

EPA selected applicants for $1.2 million to help 19 local communities integrate future site use options for cleanup of Superfund sites. In July 2000, EPA announced the selection of 40 Pilots to serve as the second round of SRI Pilots. It is anticipated that these sites will be awarded nearly $4 million.

Philadelphia Issues First Revolving Loan

The Philadelphia Industrial Development Corporation recently announced it had awarded a $300,000 cleanup loan to redevelop a site contaminated by a former dry cleaning establishment. The loan will be used by a private developer to remediate the contamination and redevelop the site into an Eckerd Drugstore. In 1997, EPA awarded a $350,000 revolving loan grant to the Department of Commerce to make low-interest loans to borrowers to clean up and redevelop brownfields projects. The Philadelphia Redevelopment Authority provided funding to assess the property.

ICMA Launches LUC Website

The International City/County Management Association ("ICMA") has launched a new online clearinghouse for land use controls. The clearinghouse will contain about LUCs imposed at brownfields and other sites with residual contamination. The website will include an electronic library of searchable documents and materials such as, case studies, reports, fact sheets, policies, guides, and other material related to the development and implementation of LUCs. The website can be accessed at www.lucs.org,

Redevelopment Project Completed at Pennsylvania Brownfield Site

Liberty Electronics recently moved into a new 46,000-square-foot manufacturing facility and office building that was constructed on a three-acre brownfield property located in Franklin, Pa. The property was formerly an asbestos plant.

The local development agency acquired the site in 1985 and demolished the asbestos plant. The agency then removed 270 tons of asbestos-contaminated soil with the new building and parking lot serving as a cap for the remaining asbestos-contaminated soil. The existing office building was transformed into a "Smart Building" known as the Emerging Technologies Center. The office building is equipped with high-speed Internet access, digital security, conference and training rooms with high-tech amenities, a sound stage and control room, clerical support

Liberty agreed to a work plan outlining how contractors would control asbestos encountered during excavation activities. A deed restriction limits the property use to industrial purposes and prohibits the use of groundwater at the site.

EPA Enters Into Prospective Purchaser Agreements

EPA entered into a Prospective Purchaser Agreement ("PPA") for the Motorola 52nd Street Superfund Site with City of Phoenix. The city plans to acquire a parcel of land comprising 0.5 acres within Operable Unit 2 of the Site as part of an expansion of Sky Harbor International Airport. Phoenix plans to use this parcel for aviation-related purposes, including airfields, terminals, parking, airport administrative functions, and air cargo and aircraft maintenance operations. The PPA indicated that the city was a PRP because of its ownership of the airport site and that the covenant not to sue ("CNTS") would be null and void if EPA determined that the city caused or contributed to the problem at the site. The CNTS would also terminate if Phoenix did not acquire the site in 18 months. In exchange for the CNTS, Phoenix agreed to pay EPA $10,000, provide an irrevocably right of access to EPA, file a deed notice advising successors in interest of the groundwater remedy, implement institutional controls. Transferees will be obligated to file an affidavit indicating that they did not cause or contribute to the release and their use will not result in a release or contribute to the migration of the existing contamination. Once EPA approves a transfer, the city would be relieved from any obligations under the PPA. However, the city will not be relieved of liability under the PPA if it leases the site. If EPA determines the affidavit of the transferee is materially inaccurate, the CNTS will be voided and not effective for the transferee. The PPA contained a lessee's certification of compliance with the PPA and the CNTS.

Though technically not a PPA, Alliant Techsystems, Inc. ("ATK") obtained a CNTS in connection with its 2000 purchase of the stock of Cordant Technologies, Inc. ("Cordant"). EPA had identified a predecessor of Cordant responsible for contamination of the Rockaway Wellfield Township Superfund Site (the "Rockaway Site"). The predecessor had entered into an administrative consent order with the NJDEP and had agreed to pay EPA's past response costs to construct a groundwater remediation system. ATK received an indemnity from the seller that included the remedial work at the Rockaway Site. ATK assumed responsibility for all other environmental liabilities. Cordant refused to pay EPA's oversight costs. In exchange for a CNTS, ATK agreed to pay EPA's oversight costs and $5,504.18 in additional EPA past response costs.

Citigroup Agrees to Settlement for Shattuck Site

A federal district court approved a settlement that resolves the liability of S.W. Shattuck Chemical Company ("Shattuck") and its corporate affiliates Philbro Resources Corporation, Salomon Smith Barney Holdings, Inc. and Citigroup, Inc. for a former radium-processing plant located in Denver.

Under the terms of the consent decree, Shattuck will pay $7.2 million for response costs and natural resources damages. In addition, Shattuck will establish a trust and convey the 5.9-acre parcel to the trust. The trustee will be obligated to sell the site that is valued at more than $1 million and then deposit the net proceeds of the sale into a special account EPA has establish for the site.

The consent decree embodies a number of provisions from the EPA model PPA. The purchaser and trustee will receive a CNTS for liability arising out of the existing contamination provided the parties cooperate with EPA and do not interfere with EPA response actions. The Shattuck's corporate affiliates also received a CNTS.

Shattuck originally paid $26 million to entomb radioactive waste within a cement cap. After community groups became concerned about the adequacy of the cap, EPA amended the Record of Decision ('ROD") to demolish the cement monolith encasing the low level radioactive materials, dispose the stabilized soil, fly ash and cement monolith debris, and to remove use restrictions imposed on the site as a result of the prior remedy.

Commentary: Citigroup Inc. became involved in this site through its acquisition of Salomon Smith Barney Holdings, Inc. ("SSBH") who had in turn had acquired Philbro Resources Corporation, a prior owner of Shattuck. SSBH had issued a corporate guaranty of Shattuck's obligations in June 2000 and a predecessor of SSBH had issued another corporate guaranty in 1993. As part of the settlement, EPA agreed that the guarantees were no longer in effect.

This case illustrates the importance of reviewing contractual obligations of a company being acquired during due diligence. The Citigroup entities might have been able to assert defenses to liability. However, like many other large corporations, the Citigroup entities felt constrained to settle this potential liability in a high profile case out of concern that they might jeopardize important relationships and incur reputation risks in an important market.

California Housing Development Halted by Contamination

In 1999, a California developer purchased 1,000 acres of undeveloped hillside in Santa Clarita where it planned to construct thousands of middle-class homes. Now, Santa Clarita LLC is looking to divest itself of the property because it cannot afford the estimated $35 million to $40 million to remediate the land.

As it turns out, the property had been used from 1934 to 1967 by a number of companies that manufactured dynamite and fireworks. From 1967 to 1987, another company manufactured and test military-grade weapons for the Department of Defense ("DOD").

When Santa Clarita LLC purchased the property, the company believed it could remediate the property by phasing in the cleanup and the construction of homes. However, the city has rejected this approach. The city believes that ammonium perchlorate is migrating into the local aquifer and has contaminated four nearby water wells. The developer says there is no proof that the site is responsible and is convinced the site does not contain any unexploded ordnance. Nevertheless, the local water utility has sued the developer over the well closings.

Meanwhile, Santa Clarita had approved a major auto mall, had planned to construct new roads and had a Metrolink station constructed near the site. Those plans are now stalled and the city is now trying to wrest control of the land from the developer under its power of eminent domain.

The Santa Clarita site is just one of thousand former military sites nationwide that may contain unexploded ammunition. For example, residents of a partly built subdivision in Arlington, Texas have found numerous World War II-era practice bombs in their yards since August 2000. More than 100 residents are suing the developer saying they were not notified that the land was located on a former test site.

In Cape Cod, nearly 1,000 pieces of buried ordnance were unearthed in 2000. The material was discovered 2,100 feet from an elementary school that had been built to accommodate a growing student population in the booming town of Sandwich.

In Denver, a planned 7,000-unit housing development on the former site of an Air Force bombing range has been stalled as the DOD struggles to clean up waste, possibly including unexploded munitions.

At another California site near Sacramento, the Army Corps of Engineers ("Corps") announced it would spend $200 million to clean up ordnance on land that was once part of the Army's Camp Beale.

Commentary: Under the Defense Environmental Restoration Program, the DOD through the Corps is authorized to identify, investigation and remediate environmental contamination at formerly used defense sites ("FUDS"). These properties were leased, used or owned by DOD or DOD contractors. Under the FUDS program, the Corps has determined that 9,181 sites were potentially eligible for the FUDS program and that 3,840 of those sites do require any further action. Recently, the GAO concluded that the Corps did not have a sound basis for determining that 1,468 or 38% of FUDS did not require any further investigation or cleanup. In "*Environmental Contamination: Corps Needs to Reassess Its Determinations That Many Former Defense Sites Do Not Need Cleanup*" (GAO-02-658, August 2002), GAO indicated that the preliminary assessments conducted by the Corps were not comparable to those performed under the federal Superfund program. For example, GAO said that the Corps overlooked or dismissed information in files that could have indicated if environmental hazards existed at the sites. GAO also said that 74% of the files reviewed did not have site maps or photos that could identify facilities that might have posed environmental threats. Moreover, the Corps did not conduct site inspections at 18% of the FUDS. The GAO also noted that the Corps is not allowed to conduct soil or groundwater sampling during its preliminary

assessments for FUDS program eligibility.

Another problem was that during the early stage of the FUDS program, the Corps focused on unsafe buildings and not the possible presence of hazardous wastes. Another failure identified by GAO was that when the Corps found contamination that was not caused by DOD activities, the property was not placed in the FUDS program and the Corps generally did not notify EPA or state environmental agencies about the contamination for 99% of the files GAO reviewed. The Corps also failed to notify current property owners of contamination in 72% of the files reviewed.

The report indicated that some FUDS officials wanted to reexamine some of the early no further action determinations but funding was unavailable. Indeed, at current funding levels, DOD estimates it will take 70 years to remediate the existing FUDS.

The report illustrates the importance of performing comprehensive historical due diligence. It also demonstrates that prospective purchasers should not simply accept the conclusions of prior environmental site assessments but critically review those reports.

County Purchases Vacant Property Source Of Contaminated Drinking Water Wells

In 1993, San Bernardino County purchased 96 acres of vacant property near the Mid-Valley Landfill to accommodate expansion of the landfill. In August 1999, the county excavated six 6 million cubic yards of dirt and dumped the soil on a portion of the vacant land, creating a 50- to 100-foot-tall mound.

It turns out the land was once used to store and dispose of explosives, and the excavated soil was placed over one of the bunkers used to store ammunition. The property is believed to be one of the sources of perchlorate contamination that has forced the closure of 19 regional drinking water wells. The state Department of Toxic Substances Control has issued a cleanup order to the county and is investigating a number of other companies that operated in the area.

Commentary: San Bernardino County asserts that it tested for explosives residue and had no knowledge that any hazardous waste were disposed at the site. Had county officials conducted sufficient historical research into the prior uses of the land, they would have been able to learn about the prior use and possibly identify the location of the former bunkers from historical photographs. Many former testing grounds were established in what was once remote areas but are now prime suburban properties. Once the prior use was discovered, it would have been advisable to collect soil and groundwater samples to characterize the extent of any contamination.

In the Santa Clarita case, the developer underestimated the extent of the contamination. With the growing popularity of brownfield programs, developers frequently assume that they will be able to remediate a property using risk-based cleanup protocols. However, even under brownfield programs, significant site characterization and cleanup will be required when the site has impacted drinking water.

Large Rural Area To Be Listed on NPL

A large rural area in Cayuga County in upstate New York has been added to the National Priorities List ("NPL"). The groundwater at the five square mile area west of Syracuse is contaminated with volatile organic compounds ("VOCs") from an unknown source. Some of the homes and farms in the affected area are not serviced by a public water supply. EPA has determined that 51 residential wells are contaminated with VOCs. The agency has installed treatment systems for the 51 private residential wells with treatment systems, installed air-stripper treatment systems at two large dairy farms and a carbon filter system at a residence that serves as a child day care facility. Many of the residences have been connected to a public water line. EPA is now concentrating on identifying the source of the contamination.

Commentary: In our last issue, we discussed the proposed ASTM Phase I ESA standard for Forested Land and Rural Property. These last two articles illustrate the importance of doing comprehensive due diligence when contemplating purchasing vacant property.

EPA To Perform Additional Cleanup At NJ Residential Property

EPA recently announced it would spend an additional $10.7 million to excavate an estimated 105,000 tons of soil from a buried creosote waste lagoon and

canal underlying a 35-acre residential community and 15-acre shopping mall located in Manville, New Jersey

In the early 1960s, 137 residences and the shopping mall were built over a former railroad tie creosoting facility in Manville, New Jersey. In 1998, EPA determined that elevated levels of creosote and other compounds were present in the soils of 86 of the 137 residential properties have to be remediated. The area was added to the NPL in 1999.

During the first phase of the cleanup, EPA more than 36 million gallons of water was pumped from the soil in a buried creosote waste lagoon located beneath eight properties. EPA then excavated an estimated 65,000 tons of contaminated soil from the area of the eight homes and 14 adjacent residences. The eight homes were demolished and residents permanently relocated while the families from the fourteen neighboring properties have been allowed to return to their remediated properties.

Commentary: Older shopping centers and residential development may have been built on former industrial properties and landfills or may have been constructed using contaminated fill material. It is important to review the historical use of the property even it the land is currently developed as residential property or for commercial use that does not appear to present a current threat to the environment. If a shopping center was constructed on contaminated fill, a cleanup may have to be performed when the shopping center is expanded or renovated.

ENVIRONMENTAL CASES INVOLVING CORPORATE AND REAL ESTATE TRANSACTIONS

EPA Seeks to Halt Sale of Asarco Subsidiary

With copper prices plunging, Asarco has defaulted on more than $450 million in outstanding loans. To reduce its $1 billion debt load, Asarco is negotiating a restructuring plan with 20 banks where the company would sell its Southern Peru Copper Corp. subsidiary to Asarco's intermediate parent company, Americas Mining Company.

However, the federal government is concerned that the parent corporation of Asarco is trying to strip Asarco of its most profitable operations and then place the company in bankruptcy so that it can avoid an estimated $1 billion in cleanup costs at nearly two dozen superfund sites across the country. Indeed, Asarco has already notified EPA that it can no longer satisfy its financial assurances requirements for its lead smelter in East Helena, Montana. Asarco told EPA that once the company's debt restructuring negotiations are complete, it would be able to use the financial test to demonstrate assurance at East Helena. As a result, the government recently filed a temporary restraining order to block the Southern Peru Copper sale. , arguing that the sale is for less the full value and would strip Asarco of its most valuable asset.

Asarco was acquired in 1999 by Grupo Mexico, one of the world's largest mining conglomerates. Grupo Mexico reported a $245 million loss last year and has a debt load of $3.2 billion. About one-third of that debt is attributed to its acquisition of Asarco. In a December 2000 reorganization, Grupo Mexico lumped Asarco including its Peruvian mining subsidiary into the Americas Mining Group. Grupo Mexico has sought to control costs by suspending operations at several Asarco smelters and sold Asarco's specialty chemicals and aggregates divisions. The Southern Peru Copper subsidiary owns two of the richest copper mines in the world. The Peruvian mines produce more copper than Asarco's mines in the United States, and their reserves are larger.

Commentary: This case is an example of the aggressive posture EPA is taking in bankruptcy cases. The agency has established a bankruptcy response team

and frequently files objections to reorganizations plans unless the plans provide for adequate resources for environmental cleanups. For example, EPA filed a proof of claim in *In re Borden Chemicals and Plastics Operating Limited Partnership et al* (DJ No. 90-11-2-875/2). In a settlement of EPA's claim, BCI, the parent of the general partner of the debtor, agreed to complete the debtor's obligations under a 1998 Consent Decree with EPA. See United States v. Borden Chemical and Plastics Operating Limited Partnership C.A. No. 94-440 (W.D. La. June 10, 1998). Under that consent decree, the Debtor agreed to obtain a RCRA permit, to come into compliance with RCRA regulations, to perform facility-wide corrective action, pay a $3.6 million civil penalty and perform certain SEPs. The Debtor applied for the permit, paid the civil penalty and began implementation of the corrective action. Under the bankruptcy settlement, the debtor will complete the SEPs, and BCI will assume responsibility for completing the corrective action and other remedial provisions of the consent decree.

States Intervene in Bankruptcy Proceedings

The Pennsylvania Department of Environmental Protection ("DEP") has established a $2 million trust fund to control mine drainage from five closed LTV mining facilities in southwestern Pennsylvania until 2003. However, additional funding will be needed for long-term operation and maintenance of the mine treatment facilities.

LTV had been maintaining the mine pools at three underground mines by continuously pumping and treating the mine drainage. After LTV filed for bankruptcy in October 2000, DEP filed claims to have funds set aside to maintain the mine drainage treatment system. In March 2001, DEP ordered LTV to make arrangements for long-term operation and maintenance ("O&M"). LTV then announced in November 2001 that it would liquidate the company by September 2002.

The funds that DEP will use to establish the trust were set aside several years ago by the last operator of one of the mines. DEP together with EPA, Ohio, New York, Indiana and Illinois is negotiating with LTV for the transfer of additional funds from the bankruptcy estate to address environmental obligations in those states.

Tenth Circuit Rules State-Supervised Cleanup Presumed to Comply With NCP

The Court of Appeals for the Tenth Circuit reversed a district court ruling refusing to allow a property owner to bring a cost recovery action for costs incurred under a state consent decree. The district court had held that the plaintiff's cleanup performed under state supervision pursuant to the EPA "state deferral pilot program" had not been consistent with the National Contingency Plan ("NCP").

In *Morrision Enterprises v. McShares Inc.* (10th Cir. No.98-3219, 8/1/02), the defendant had supplied grain fumigants to the plaintiff for use at the grain elevator facility from the 1950s until approximately 1985. The liquid grain fumigants contained carbon tetrachloride. In November 1963, a spill of the fumigants occurred when a defendant's employee was preparing to unload fumigant for delivery to the plaintiff.

In 1988 the Kansas Department of Health and Environment ("KDHE") tested residential water wells on property adjacent to the plaintiff's property and determined that the water in those wells was contaminated by carbon tetrachloride. The plaintiff provided alternative water supplies to the residents and KDHE issued an administrative order requiring the plaintiff to investigate the carbon tetrachloride contamination on its property. By June 1997, the plaintiff had incurred $ 430,000.

The district court found that plaintiff had performed all activities required under the KDHE Consent Order and that the costs were otherwise reasonable and necessary. Nevertheless, the court concluded that because plaintiff had been unable to call any expert witnesses on its behalf to establish consistency with the NCP, the plaintiff had failed to meet its burden.

On appeal, the plaintiff argued that the district court should have granted it a presumption of NCP compliance because the cleanup was performed under a state approved consent decree. The Tenth Circuit noted that EPA had determined that sites remediated under the deferral program were being handled in a manner consistent with the NCP. Thus, the court concluded that the plaintiff was entitled to a rebuttable presumption of compliance with the NCP

based on the fact that its actions were undertaken pursuant to a consent order with the KDHE.

 The Schnapf Environmental Report is a bi-monthly newsletter which provides updates on regulatory developments and highlights significant federal and state environmental law decisions affecting corporate and real estate transactions, and brownfield redevelopment. The newsletter is published by Law Professor Lawrence P. Schnapf, 55 E.87th Street, #8B, New York, New York 10128. Telephone: (212) 996-5395. Fax: (503) 213-9314. E-Mail: LSchnapf@environmental-law.net. Subscription rate for the Schnapf Environmental Report is $99 for one year (six issues) or $25 per issue.

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 $99. 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 contact Lawrence Schnapf.

The information contained in this newsletter is not offered for the purposes of providing legal advice or establishing a client/attorney relationship. Environmental issues are highly complex and fact-specific and you should consult an environmental attorney for assistance with your environmental issues.