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A Newsletter Covering Recent Environmental Developments and Caselaw

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The Schnapf Environmental Journal is a bi-monthly report that provides updates on regulatory developments and highlights significant federal and state environmental law decisions affecting corporate and real estate transactions, and brownfield redevelopment. 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.

DUE DILLIGENCE/AUDITING

Riskier Properties Appeal To New B Buyers

With long-term interest rates still low and the stock market generating paltry returns, new players are entering the securitization market to take advantage of the high yields offered by the so-called B-pieces. These new investors appear to be more willing to purchase the B-piece debt that have become too risky for the investment firms that had dominated the commercial mortgage-backed securities (CMBS) market.

The $550 billion CMBS market has its origins in the real estate collapse of the late 1980s and early 1990s when the Resolution Trust Corporation (RTC) began packaging mortgages as securities with different risk levels. To create the securities, investment banks pool a variety of mortgage loans into bonds that typically have low-grade or unrated loans commonly known as “B pieces” that often have annual yields of 20%. The B-pieces usually consist of run-down commercial properties such as strip malls, old office buildings and hotels. As with so-called junk bonds, the risk to the B-piece is that the loans will default and they will not be able to recoup their investment or be forced to take title to an under-performing property.

The B-piece market has been dominated by four firms--GMAC Institutional Advisors, ARCAP REIT, CW Capital (formerly Allied Capital Corp.) and LNR Property Corp.

These four investment firms, who have been coined “the cartel” by bond issuers, purchased virtually all of the riskiest portions of the bond issues. Due to the risk and the fact that the bonds cannot be sold without the B-piece buyers, B-piece players have exercised considerable influence over the makeup of the bonds and have demanded extensive information about the loans, particularly environment issues. Typically, B-piece buyers have rejected 10% of the loans in a pool.

The new B-piece players are showing a willingness to purchase bonds that have higher default risks, including contaminated properties. Indeed, according to the Wall Street Journal, the four established B-piece buyers only purchased 50% of the CMBS issued in 2004.

Commentary: *As a result of this influx of new B-piece investors, mortgage originators and bond issuers are showing a greater willingness to consider contaminated properties that might have not been considered for the CMBS market in the past. This trend not only presents a new business opportunity for environmental consultants, but also a potential for greater risk. Properties that seemingly may have benign current uses, such as retail centers, restaurants and even mobile home parks, could have had environmentally sensitive operations in the past. Consultants must carefully assess the past uses of a*

property. They should determine if dry cleaners operated in the past at a shopping center, make sure a donut shop on a corner property was not formerly a gas station and verify if heating oil tanks may have been formerly located at a commercial or residential complex. If a cleanup was performed in the past, verify if there were any reopeners associated with the no further action letter and if there are any institutional controls and/or engineered controls that need to be maintained. If a property is enrolled in a state dry cleaner or UST program, remember that these state programs are focused on limiting expenditures and only addressing immediate health or safety risks. If a property has a low ranking and will not be remediated for several years because groundwater is not being used for drinking water, be sure to consider if there could be a risk of vapor intrusion that the state fund has not considered. Due to the frenetic pace of the CMBS market, consultants are under enormous pressure to produce Phase I ESA reports on potentially contaminated properties in a relatively compressed period of time. The combination of truncated review periods, incomplete historical information and presence of potential contamination can provide ample opportunity for errors and lawsuits if the environmental site assessment reports fail to identify potential environmental issues. As the following cases and discussions illustrate, lawsuits against consultants are on the rise.

New York State Court Allows Claim To Proceed Against Environmental Consultant Despite Limitation of Liability Clause

In 1999, Mercy Center, Inc. (Mercy) agreed to purchase a vacant lot in the Bronx, New York from the New York City Economic Development Corporation (NYCEDC). Mercy, a non-for-profit organization, planned to construct a center to provide guidance and assistance to mothers of school-age children including domestic violence counseling, English-language education as well as employment preparation and placement. Mercy agreed to purchase the property "as is" and to waive any claims against NYCEDC arising out of the presence of hazardous substances on the property.

In November 1999, Mercy retained JLC Environmental Consultants, Inc (JLC) to perform a Phase I environmental site assessment (ESA) in accordance with ASTM E1527. During its investigation, JLC observed fill ports believed to be associated with a former underground storage tank (UST) and noted that one of the historical maps for the property had indicated the presence of a gasoline UST. The immediate prior use of the property had been as a parking lot.

In response, JLC recommended that ground penetrating radar (GPR) survey be performed to try to determine if the UST was still present on the site. Mercy entered into a second agreement with JLC for the GPR survey. Both JLC agreements limited the firm's liability to the $2,980 fee

paid for the environmental assessments.

JLC retained Advanced Cleanup Technologies (ACT) to perform the GPR study. ACT prepared a report that indicated the GPR found that the gasoline fill ports were attached to piping that extended for two feet underground and that there was no other evidence of USTs. JLC then issued its Phase I ESA report in June 2000 that concluded that no petroleum tanks were observed and that the GPR did not reveal any USTs. The ACT report was attached the JLC ESA.

Shortly after Mercy closed on the property, a contractor encountered three USTs and contaminated soil during excavation for the foundation. Mercy spent over $259K to remediate the contamination and incurred over $100K in additional construction costs. Mercy then filed a lawsuit against both JLC and ACT for breach of contract, gross negligence and negligent misrepresentation.

JLC filed a motion to dismiss the negligence claims and sought summary judgment on its affirmative defense of the contractual limitation of liability. In an unreported decision, the Supreme Court for the County of New York found that under the economic damages doctrine, Mercy was limited to a breach of contract action and dismissed the negligence claims (Mercy Center, Inc. v. JLC Environmental Consultants, Inc. and Advanced Cleanup Technologies, Inc., No. 600476/03, July 25, 2005).

On the breach of contract claim, Mercy introduced expert testimony indicating that JLC's environmental assessment fell below industry standard. The expert testified that a qualified GPR survey contractor should have used additional geophysical equipment such as electromagnetic metal detectors, magnetometers and radio-frequency utility-locating instruments in conjunction while performing the GPR survey. The expert also said that the GPR survey report failed to accurately discuss the limitations of what a GPR survey could accomplish. Given the past use of the property and the existence of the fill ports and piping, Mercy's expert concluded that JLC should have recommended a Phase II investigation.

The court ruled that it was a factual issue as to whether JLC breached its contract by failing to comply with industry standards. As to the limitation of damages defense, the court said a contracting party can absolve or limit its damages from its ordinary negligence, but may not contractually limit itself from the consequences of its gross negligence. Since there was a material question of fact whether JLC was grossly negligent in the performance of its contract or in hiring ACT, the court denied JLC's motion for summary judgment.

Several months later, ACT filed its own motion for summary judgment, asserting that it owed no duty to Mercy since ACT had been retained by JLC and therefore had no contractual relationship with Mercy. However, the court ruled that New York law provided that a defendant may be liable for pecuniary damages arising out of negligent misrepresentation if there is actual privity of contract or a

"relationship so close as to approach that of privity." To prove the requisite relationship, a plaintiff must demonstrate that the defendant was aware that the reports would be used for a particular purpose, reliance on the report by a known party in furtherance of that purpose and some conduct by the defendant linking it to the known party that evinces defendant's understanding of the reliance.

The court said Mercy was not a member of the general public seeking to rely on the report, but a party having an ownership or prospective ownership interest or responsibility for the surveyed property. Moreover, the court said the law did not require ACT to know the precise name of the party relying on the report, just that such an individual exists. Since ACT was aware that a prospective purchaser of the property would use its report, the count dismissed ACT's motion for summary judgment.

Commentary: *Both of these rulings are significant for borrowers and lenders. Consultants often place limitation of liability clauses in their contracts. The JLC decision illustrates that these clauses may not operate if the plaintiff can show that the consultant was grossly negligent. Of course, a plaintiff has to meet a fairly high threshold to sustain a gross negligence claim, introducing evidence that the defendant's conduct constituted reckless disregard for the rights of others.*

The ACT decision is perhaps more significant because it could possibly establish a path to convince a court to ignore reliance language in a contract. Under the rationale of this decision, a consultant retained by a lender could be liable to a borrower if the consultant is aware of the purpose of the report, namely, to finance the acquisition of the property or refinance a loan of an existing property owner. In addition, the decision can provide an avenue for relief for lenders when a consultant directly hires a subcontractor to perform an aspect of due diligence and who does not have any direct contractual relationship with the lender.

Municipality Fails To Establish Consultant Breached Standard of Care For Failing To Identify Contamination

In 1997, Montville Township (Montville) entered into an agreement with a developer who planned to construct single-family homes on a 130-acres of agricultural land. As part of this agreement, Montville agreed to pay $2.2 million for 100 acres that would be designated as open space. The acquisition price was to be funded principally by a grant from Morris County (County). Since a satisfactory Phase I ESA was a pre-condition of the grant, the County retained Post, Buckley, Schuh & Jernigan, Inc. (PBS&J) to perform the Phase I ESA. The PBS&J May 1998 report identified an "accumulation of abandoned motor vehicles, tires, tanks, construction debris, household debris, and other abandoned items."

Montville and the County required removal of the debris as a condition of closing. Montville then hired Princeton Hydro, LLC

(Princeton) to perform a subsequent inspection of the area and ensure that the seller and developer had removed the debris. In May 1999, Princeton reported that the areas of concern had been addressed. In reliance on the Princeton report, Montville's planning board authorized the subdivision of the property and the acquisition of the open space portion of the property. Montville acquired title in July 1999.

In December 1999, Montville learned the areas of concern identified in the PBS&J May 1998 report had not been addressed. Montville hired a third contractor, Maser Consulting (Maser), to perform a Phase II investigation. Maser detected DDT, lead, and arsenic present at levels above the commercial and residential clean up standards imposed by the New Jersey Department of Environmental Protection (NJDEP). After the developer and former property owner refused to clean the property, Montville entered into a memorandum of agreement (MOA) with the NJDEP.

Montville initially brought a variety of statutory and common-law contribution and indemnification claims against the seller and developer. The federal district court denied the CERCLA contribution claim on the grounds that the NJDEP MOA was not a settlement under section 113(f)(3) of CERCLA (see Aviall update story below for more detail on this issue).

The township then focused on PBS&J, asserting that the firm failed to identify the existence of a known hazardous substance on the property and failed to exercise reasonable care in preparing the Phase I ESA report and the performance of its duties. Montville noted that the introduction of PBS&J's report stated that the contract objectives were to "determine if current or past land use practices have adversely impacted the site, to identify any other potential environmental concerns, and to determine if additional field investigations are warranted." As a result, Montville argued that PBS&J's failure to achieve those objectives constituted a breach of contract because PBS&J recommended that no soil sampling be performed on the property prior to closing.

PBS&J moved to dismiss the complaint because Montville had failed to file an Affidavit of Merit pursuant to N.J.S.A. 2A:53A-26. Montville countered that PBS&J's failure to test the soil or discover the hazardous chemicals during the Phase I analysis constituted a breach of contract, as opposed to professional malpractice, and therefore was beyond the purview of the Affidavit of Merit Statute.

In Montville Township v. Woodmont Builders, et al, 2006 U.S.Dist. LEXIS 514 (D.N.J. January 5, 2006), the federal district court for the district of New Jersey said to show that PBS&J breached its contractual duty, Montville had to prove that PBS&J's conduct fell below the industry standard of care when PBS&J failed to recommend that soil sampling be performed. The court said the industry standard would be measured by the guidelines established by the American Society of Testing and Materials, the Federal National Mortgage Association

("Fannie Mae"), the Federal Home Loan Board, and the New Jersey Department of Environmental Protection's Technical Requirements for Site Remediation (N.J.A.C. 7:26E) since these were referenced in the introduction to PBS&J's report.

PBS&J contended that when the Phase I assessment was performed in 1998, concern for soil contamination from prior agricultural uses was not yet an issue of concern in the New Jersey environmental consulting community. Although the claim was labeled as a "breach of contract," the court said the essence of Montville's claim was professional malpractice. Because the underlying factual allegations require proof of a deviation from the professional standard of care, the court held that this dispute was a question of fact that could not be determined by a layperson, but required expert testimony. Therefore, since Montville failed to file an Affidavit of Merit, the court granted PBS&J's motion to dismiss.

Insurer Not Obligated To Indemnity Consultant For Failing To Discover Contamination

When are damages sustained as a result of alleged breach of contract by an environmental consultant for purposes of determining insurance coverage? Is it when the consultant performed the professional services or when the client actually incurs remediation costs? This was the issue before a Louisiana state court in Herzog Contracting Corporation v. Robert V. Oliver et al., 2005 La. App. LEXIS 2581 (Ct. App.-2nd Cir. December 16, 2005).

In 1988, Herzog Contracting Corporation (Herzog) retained Geotechnical Testing Laboratory (GTL) to perform a Phase I ESA I on a former creosote wood treatment facility that Herzog contemplated purchasing. GTL concluded that the site was "free of contamination and no extensive cleanup operations are anticipated in order to utilize this site for commercial construction." GTL added that "if any contamination was present, it would not likely result in remediation."

In 1991, the Louisiana Department of Environmental Quality (DEQ) discovered the presence of hazardous substances during an investigation prompted by a citizen's complaint. The source of the contamination allegedly came from creosote wood treatment operations conducted on the site prior to 1983.

Herzog then filed an action against the seller as well as GTL, claiming that GTL breached its contract when it failed to discover the contamination. Herzog sought damages from GTL for the alleged breach, including reimbursement for all sums paid by Herzog for the property and all sums paid by Herzog for remediation of the site, as well as costs and attorney fees. GTL denied that Herzog had retained it to perform or conduct an environmental survey, investigation, assessment or evaluation of the site. Instead, according to GTL, the scope of its work for Herzog was limited to the following: taking soil borings in locations selected by Herzog and in the manner and to the depths specified by Herzog; having the soil

samples tested by a laboratory for the presence of contaminants specified by Herzog; and reporting the results of the laboratory tests to Herzog. GTL claimed that the work which it performed was done under the supervision, direction and control of Herzog and denied any liability to Herzog. GTL then filed a third party complaint against general comprehensive liability insurers, the Maryland Insurance Company, the Maryland Casualty Company, and the National Standard Insurance Company (Maryland Defendants) to recover the costs to defend the suit and any damages it might be required to pay Herzog. After denying coverage and any obligation to defend the suit, the Maryland Defendants filed a motion for summary judgment seeking dismissal of all of GTL's claims, as well as the claims of Herzog.

The insurers argued the professional services endorsement contained in the Maryland Defendants policies excluded coverage for bodily injury or property damage due to the rendering or failure to render any professional service. Because the code used in the endorsement was for "analytical chemist," GTL contended that the exclusion did not apply because it only collected samples and had the actual chemical analysis of the soil performed by an outside laboratory. In December 2001, the trial court granted summary judgment for the Maryland Defendants, holding that Herzog retained GTL to perform an environmental assessment that included an analysis of the soil conditions to determine the presence of chemicals related to the prior creosote plant operations. The court said the fact that GTL may have subcontracted part of the actual laboratory testing to another firm did not diminish its role or eliminate its obligation to provide the analysis of the soil, including the chemical composition, the results of which it analyzed and reported to Herzog.

GTL then turned its attention to the policies issued by West American Insurance Company (West American) from September 1, 1995 to September 1, 1998. The policies defined property damage as physical injury to tangible property or loss of use of the property. GTL argued that the damage was contamination that still existed during the policy period and that Herzog was unable to use the property for its intended use until the contamination was remediated.

West American filed a motion for summary judgment on grounds that the property damage did not occur during the policy period. The trial court granted the insurer's motion for summary judgment and the appellate court affirmed. The court noted that previous owners and users of the site caused the contamination resulting in physical injury and loss of use, so that the property damage occurred prior to the inception of the policy. However, even if the property was not physically injured, the policies linked the loss of use to an "occurrence." Because Herzog alleged that GTL breached its contract and was negligent in failing to discover contamination, the occurrence that would have triggered coverage under the West American policies was when GTL allegedly failed to properly perform the environmental

investigation. Since the environmental assessment was performed in 1988, which predated the West American policies by seven years, the Court ruled there was no occurrence during the term of the West American policies.

Contamination Discovered During Refinancing

Borrowers and mortgage originators often wonder why it is necessary to repeat sampling on a property that is being refinanced or has already gone through securitization. They feel if the prior lender found the property acceptable, why should the new lender require further investigation. A recent decision of the federal district court for the district of New Jersey provides some insight.

In Norkus *Enterprises, Inc. v. Getty Oil Company, Inc*., 2005 U.S. LEXIS 29262 (D.N.J. November 21, 2005), Tidewater Oil Company (Tidewater) owned and operated a gas station from 1935 to 1967. Getty Oil took title to the property by merger with Tidewater in 1967. Shortly thereafter, Getty conveyed the site to Harry and Minnie May who, in turn, sold the property to Neptune Gardens Supermarket, Inc., (Neptune) in 1969. At the time that Neptune acquired the site, it was used as an asphalt parking lot. Neptune then constructed and operated a supermarket on the site until the 1970s when Norkus Brothers, a predecessor to the plaintiff, acquired Neptune.

The property was financed numerous times over the years without any concerns about the site's prior use. In connection with a 1999 refinancing, the plaintiff was required to perform a Phase II ESA investigation and the soil sampling did not identify gasoline or other contaminants associated with its former use. However, when the plaintiff tried to refinance in 2002, the lender required that the Phase I ESA include a GPR survey. Four USTs were identified beneath the parking lot and contaminated soil was encountered when the tanks were excavated. An analysis of the gasoline determined that it had been released prior to 1986.

In 2004, the plaintiff brought a contribution action under the New Jersey Spill Compensation and Control Act (Spill Act) for reimbursement of its costs and mandatory injunctive relief requiring the defendant to complete the cleanup. The defendants filed an answer asserting that the claims had been discharged by the 1991 Texaco bankruptcy (Texaco had acquired all of the assets of Getty in a 1984 transaction that resulted in a high-publicized $10.5 billion verdict against Texaco in 1987). The defendants also moved to have the action transferred to the bankruptcy court. Because the bankruptcy court had retained jurisdiction for all matters pertaining to the Texaco bankruptcy, the federal district court in New Jersey agreed to transfer the venue to the federal district court for the southern district of New York.

Commentary: *When reviewing prior Phase II reports, it is important to review old maps and other historical records to determine where prior structures such as USTs and dry*

cleaning equipment may have been located and then to verify that the samples were collected from the areas of concern. If the samples are not properly located, the laboratory results may not be representative of sub-surface conditions in those areas of concerns.

Consultant Liable As Discharger Under New York Oil Spill Law For Inadequate UST Cleanup

A New York state court ruled in *Breslau v. Palma* (Index No. 12659/2001, Nassau Cty. Sup. Ct. 11/29/05) that an environmental consultant could be liable as a discharger under Article 12 of the state Navigation Law (a/k/a Oil Spill Act) for failing to prevent petroleum contamination from migrating beneath a neighbor's home after removing a leaking home heating oil tank.

In this case, the plaintiffs detected the smell of oil in their home in Massapequa Park, NY in September 1996. They notified their oil supplier who determined that there was oil in the ground between their home and the Palma property. In December 1996, a spill was reported to the New York State Department of Environmental Conservation (NYSDEC). The agency performed an investigation and confirmed that the source of the contamination was the defendants' leaking home heating oil tank. In January 1997, the defendants hired Allied Construction to remove their tank, which was found to have holes in it and to be leaking. The Palmas notified their insurer, Chubb Indemnity Insurance Company (Chubb) who retained defendant Fenley & Nicol Environmental, Inc., (Fenley & Nicol) to investigate and remediate the contamination. In early 1997, Fenley & Nicol excavated contaminated soil from the Palma property and backfilled the excavation with clean fill. Fenley & Nicol also installed monitoring wells on both the Palma and Breslau properties that were to be periodically monitored by Fenley & Nicol. By mid-1998, though, the Breslau's noticed a puddle of petroleum contamination seeping through their basement floor and soaking the rug on the floor. In addition, the petroleum odors grew worse. When situation failed to improve, Fenley & Nicol was replaced with Anson Environmental, Ltd. (Anson). Anson discovered higher levels of contamination in areas near the original tank source than previously reported by Fenley & Nicol, and located additional petroleum in areas that had been overlooked.

The Breslau's then filed an action seeking to hold the Palmas, Chubb and Fenley & Nichol liable for damages to their property under the Navigation Law. The court noted that dischargers are strictly liable under the Navigation Law and that this liability extends to both landowners who can control activities occurring on their property as well as contractors hired to remediate contamination, but fail to prevent continuing contamination.

Fenley & Nichol argued that it should be entitled to liability immunity as a responder under section 178-a of the Navigation Law. However, the court ruled that the responder

immunity was only applicable to discharges of petroleum into or onto navigable water. Since there was no evidence that the oil spill had impacted any navigable water, the court held that the defense was not available. The court then granted summary judgment to the plaintiffs against all defendants on the Oil Spill Act cause of action.

Commentary: *The court's reasoning for denying the responder immunity defense was strained. The liability sections of the Navigation Law have been applied to petroleum discharges to soil and groundwater even though the law was enacted in 1977 to protect against the impacts of oil spills from offshore oil platforms that were under consideration because of the oil shock of the 1970s. There is no textual justification for expanding discharger liability to groundwater that is clearly not "navigable," but limiting the responder defense to navigable waters. It can also be considered very bad public policy since every consultant remediating contamination from leaking UST may be potentially liable for the continued migration of contaminants that remain in the soil or groundwater. This decision could discourage the use of risk-based cleanups for petroleum sites in New York as consultants will be afraid that they may become liable for additional cleanup if residual contamination does not naturally degrade as contemplated, but instead begins to migrate or even pose a risk of vapor intrusion.*

This decision follows an aggressive initiative by NYSDEC and the New York State Comptroller's Office, which is responsible for administering the state Oil Spill fund for untimely or incomplete reporting of petroleum discharges. In 1998, an administrative law judge (ALJ) upheld a penalty assessment levied by the NYSDEC against a lender's consultant for failing to report evidence of a leaking a UST that was being removed by a borrower's contractor. The ALJ reasoned that the bank's consultant was obligated to disclose the oil he observed leaking through holes in the tank as it was lifted from the ground because the NYSDEC regulations governing petroleum storage tanks impose a reporting obligation on "anyone" who has knowledge of a spill. Recently, two Manhattan cooperative apartment complexes were fined over $1 million each for allegedly failing to report oil spills associated with heating oil located in the basements of the buildings.

There is also considerable confusion about the status of aboveground tanks situated in concrete vaults located in basements or other below ground rooms. If the tank cannot be accessed or inspected, it will be considered a UST that must undergo periodic tightness testing. It is also important to consider the condition of fill pipes serving tanks that are regulated as ASTs. Fill ports located at the curb of the street are problematic since piping that runs beneath the sidewalk often leaks and petroleum can migrate through basement walls or to other buildings depending on bedrock faults, utility conduits and neighborhood topography. Many apartment buildings have floor drains and sumps located in their basements that discharge into the

city sewer system. State regulators will view oil flowing into these floor drains or sumps as discharges to surface water that can result in significant fines and cleanup costs. As a result, it is important for consultants, potential building owners and their lenders to carefully assess the condition and regulatory status of heating oil tanks in buildings during environmental due diligence.

Rhode Island and New York Courts Rule Incomplete Property Disclosure Forms Do Not Give Rise to Breach of Contract Actions

Many states have enacted laws requiring sellers of residential property to provide purchasers with a disclosure statement that provides information on a variety of property conditions, including underground storage tanks. However, as the following cases illustrate, these disclosure laws do not necessarily alter the traditional common law doctrine of *caveat emptor* (buyer beware) nor provide buyers with significantly new remedies for undisclosed conditions.

In *Caseau v. Belisle*, 2005 R.I. Super. LEXIS 144 (Sept. 26, 2005), the plaintiffs agreed to purchase a four-acre parcel for $179K in February 2001. When they inspected the property, it was covered with snow. They asked what was below the snow in the yard and the defendant told them sod. They also asked if anything was buried below a shrine to the Blessed Virgin and were told nothing. When the snow began to melt after the March closing, the plaintiffs discovered tires and waste materials strewn on the ground, partially buried or completely buried. Claiming that the cost to remove the assorted debris would exceed the cost of the purchase price of the property, the plaintiffs filed a lawsuit against a number of parties including the sellers, charging that the defendants had actual or constructive knowledge of the condition of the property and had failed to disclose the conditions in the property disclosure form. They sought rescission of the contract, return of their purchase price, damages for diminution of property value and compensatory damages for the costs to remove the debris. Following three years of discovery and a five-day trial, a jury awarded the plaintiffs $103,400. Arguing that the jury's verdict was against the weight of the evidence, the defendants moved for a new trial. However, the court ruled that the defendants only had a duty under common law to disclose abnormally dangerous conditions and that the plaintiffs had not introduced any evidence showing that the debris created an unreasonable risk of harm.

On the breach of contract claim, the court noted that the statute requiring preparation of a property disclosure statement did not alter the common law of *caveat emptor* and was intended only to affect the negotiations and dealings between parties prior to the closing. The court said that the disclosure statement was not a part of the contract, was not a warranty of any deficient conditions and did not constitute contractual promises. Since none of the representations made in the

disclosure form were incorporated into the agreement and the doctrine of merger provides that the acceptance of a warranty deed extinguishes any representations in a contract, the plaintiff could not prevail on its breach of contract claim. Moreover, the court noted that the statute specifically stated that buyer should not solely rely on the statements in the disclosure form, but conduct its own investigation. In addition, the seller was under no affirmative obligation to conduct an inspection prior to preparing the disclosure form. The court did indicate that statements in a disclosure form could serve as a basis for a claim for fraud or misrepresentation. The court said there was a material factual dispute as to the extent that the defendants were aware of the buried debris or even if the few visible tires constituted a deficient condition that had to be disclosed. The court granted the defendants' motion for a new trial on the fraud or misrepresentation cause of action.

New York has a property disclosure statement law similar to Rhode Island; both laws state that they do not diminish the responsibility of a buyer to carefully examine a property prior to purchase. The New York law does provide that the buyer is entitled to a $500 credit if a seller fails to timely submit a disclosure form or provides an incomplete form. A state court recently dismissed claims brought by a buyer in *Gabberty v. Pisarz*, 2005 N.Y. Misc. LEXIS 2535 (Nassau Sup. Ct. Sept. 22, 2005) where a seller failed to disclose a chronic water seepage/basement flooding condition. The seller's wife prepared the disclosure statement and left a series of questions about rot, water seepage and drainage problems unanswered. The plaintiff charged that it was entitled to its actual damages because the seller had willfully failed to perform its obligations under the law. The court said to maintain the statutory claim, the plaintiff had to show a deliberate misstatement regarding a defective condition that would tend to assure a reasonably prudent buyer that no such condition existed and that a professional inspector might not discover during an inspection that met industry standards. The court found that the disclosure statement with omissions about water intrusion should have put her on notice to inquire further about this issue consistent with her responsibility under common law. Moreover, the court noted that there was no provision in the law for automatically incorporating statements contained in the disclosure form into a contract. Because the contract contained an "as is" provision and acknowledged that the buyer was thoroughly acquainted with the condition of the property, the court held that the plaintiff was not entitled to any damages aside from the $500 credit for seller's failure to provide her with a completed disclosure statement.

Commentary: *Because of the statutory $500 credit, many attorneys advise sellers to simply provide the purchasers with a $500 credit instead of preparing the disclosure form and running the risk of possibly facing a claim for misrepresentation in case the statement turns out to be*

incomplete or inaccurate. The Gabberty court did suggest in dicta that such a practice might amount to willful failure to perform the requirements of the law. Until a court expressly rules on this issue, buyers should carefully evaluate conditions of properties, particularly heating oil tanks, asbestos and water intrusion that could lead to mold growth. Buyers should also try to incorporate statements into the disclosure form in their contracts although this can be difficult to negotiate in a sellers market.

Should Vapor Intrusion Be Considered a REC?

One of the more interesting issues to emerge from the first meeting of the ASTM Task Force on Vapor Intrusion (E 50.02.06) was whether the presence or potential for the presence of vapor intrusion should be identified as a Recognized Environmental Condition (REC) in Phase I Environmental Site Assessments. The answer could have enormous professional liability implications given the thousands of environmental assessments that have relied on pre-2000 no further action letters or Phase II ESA reports that probably did not examine the vapor intrusion pathway.

Those who feel that vapor intrusion is a REC argue that vapor intrusion constitutes a release of a hazardous substance or petroleum product into a building structure since the vapors themselves are the gaseous form of the contaminant provided the concentrations are at levels that would be hazardous to human health. If the levels are below the indoor air target concentration, the general view of those in this group was that it would then be considered a de minimis condition. Another reason postulated for addressing the vapor intrusion pathway separately was that the pathway is not always directly related to impacts to groundwater, but can be influenced by subsurface geology or other factors that can cause vapors to migrate onto a property from an off-site source.

The contrary view was that releases of contaminants into indoor air are excluded from the definition of a CERCLA release and therefore cannot be a REC under ASTM E1527. Those in this camp felt that vapor intrusion should be treated like other indoor air quality issues, such as radon or asbestos, that are non-scope items under ASTM E1527 and can be added at the request of a client. One example to support this view was indoor air emissions from equipment in a workplace. If the emissions source was regulated by OSHA or the Clean Air Act, it should not qualify as a REC since CERCLA did not apply.

Another view was that RECs as releases were limited to releases to soil or groundwater; but where a state required remediation activities to potential vapor intrusion to structures, the Phase I ESA report should assess the potential for vapor intrusion.

Commentary: *A related question was what search criteria would an environmental professional have to use to determine that the vapor intrusion pathway did not potentially impact a site. The EPA 2002 draft*

vapor intrusion guidance suggests that the vapor intrusion pathway should be assessed if a property is located within 100 feet of one of the contaminants of concern identified by EPA in its guidance. Does this mean the consultant only has to search within a 100-foot radius for adjacent properties that currently or formerly used such contaminants of concern? EPA did caution in the VI guidance that the distance might have to be increased under certain conditions such as a preferential pathway or large area of impermeable surfaces that could lead to the accumulation of vapors and migration through molecular diffusion, or density-driven vapor clouds.

A number of lawsuits related to vapor intrusion have been filed, including several against consultants who failed to identify vapor intrusion as a potential concern. Until a commonly accepted industry standard for vapor intrusion emerges, and in the absence of state regulations or guidance, consultants should carefully consider if releases of chlorinated solvents or petroleum at or within proximity of a site could pose a potential for vapor intrusion and indicate whether further investigation is warranted.

Should OSHA Standards Be Used to Determine Risks Posed by the VI Pathway?

One of the more vexing questions involving vapor intrusion is whether the permissible exposure levels (PELs) established by the Occupational Safety and Health Administration (OSHA) for chemicals used in the workplace should be used when evaluating the risk posed by a vapor intrusion pathway.

OSHA promulgated its PELs primarily on the Threshold Limit Values adopted by the American Conference of Governmental Industrial Hygienists (ACGIH) in 1968. As a result, the PELs are less stringent by several orders of magnitude than the risk-based concentration used by EPA and the states for vapor intrusion that are generally based on a risk threshold of a incremental cancer risk of one in a million. Because of the significant differences between the PELs and the indoor air target concentrations under the various VI programs, active facilities have argued that the OSHA PELs should be the applicable standards for determining if the VI pathway needs to be investigated and if remedial actions are required.

EPA's 2002 Draft VI Guidance explicitly states that it is not applicable to "occupational settings" since such workplace exposures are subject to the PELs, but the meaning of what constitutes an “occupational setting” is not very clear. EPA considers occupational settings to include workplaces where workers are handling hazardous chemicals *(e.g.,* manufacturing facilities) similar to or different from those in the subsurface contamination, as well as other workplaces, such as administrative and other office buildings, where chemicals are not routinely handled in daily activities. Nevertheless, EPA recommends that such facilities be notified of the potential for this exposure pathway and that they consider any potential exposure that may result.

EPA also indicated that the VI

Guidance may apply in occupational settings where the chemicals presenting a risk of vapor intrusion are no longer or never were used in the workplace, or where chemicals were modified by degradation. In addition, the guidance indicates that a change in use may trigger pathway reevaluation and that the PELs are not ARARs for purposes of remedy selection.

Perhaps the most difficult scenario is non-residential settings where persons are in a non-working situation. EPA indicated that non-residential buildings might need to be evaluated where people (typically non-workers) may be exposed to hazardous constituents entering into the air space from the subsurface. This setting applies to buildings where the general public may be present such as schools, libraries, hospitals, hotels, and stores. However, EPA recommends that appropriate adjustments be made for nonresidential exposure durations, the building specific air volumes and air exchange rates, as well as other relevant factors to be considered.

In April 2001, EPA Region 1 office issued draft guidance stating that the PELs may be appropriate when a facility is operated "with full actively maintained knowledge that releases from current and past operations exist which may contribute to current indoor air concentrations." However, the Region 1 office indicated that it would use the lowest value available under PELs or recommended Exposure Levels (EL) set by the National Institute for Occupational Safety (NIOSH), and the most recent ACGIH Health and Threshold Limit Values. EPA Region 1 said it would use OSHA-related guidance because of OSHA's "inability to revise or update their regulatory standards." EPA Region 1 indicated that it would cut OSHA standards and guidance by a factor of 100 for the RCRA Corrective Action program. In other words, the EPA office would use 1% of the OSHA levels as the interim standards for determining if the EL has been achieved. EPA Region 1 justified this reduction on the basis that remediation of soils cannot be accomplished as quickly as repairing industrial sources of indoor air within a workplace. The regional office also indicated that it expects facilities to strictly comply with all OSHA controls involving monitoring, training and employee awareness. However, EPA region 1 emphasized that OSHA standards and guidance would not be used for selecting corrective action standards for soil or groundwater.

Commentary: *OSHA proposed revisions to its PELs in 1989 after concluding that they were not sufficiently protective (54 FR 2333, January 19, 1989) and that there were no PELs in existence for many toxic chemicals that were commonly used in the workplace. The rule lowered the PELs for 212 substances and created new PELs for 164 substances that had not been previously regulated by OSHA. However, a labor union challenged the rule on the grounds that the exposure limits for many of the 428 substances covered by the rule were not sufficiently protective. In AFL-CIO v. OSHA, 965 F.2d 962 (11th Cir. 1992), a federal appeals court vacated the standards and sent it*

back to OSHA for further review.

EPA and OSHA did enter into an MOU in 1990. The document defines the respective roles of the agencies in identifying and addressing environmental and workplace hazards. EPA will have authority over significant adverse reactions to chemicals posing potential hazard to public health or environment; accidental, unpermitted or deliberate releases beyond workplace; and violations of EPA regulations. OSHA, in turn, generally will take the lead role in addressing occupational exposures. The MOU also provides that agencies will notify each other if their inspectors identify discover of violations of the other agency's requirements.

According to a report in InsideEPA in 2004, OSHA apparently concluded that it was prohibited under the OSHA general duty clause from preventing EPA from addressing risks posed by the vapor intrusion in OSHA regulated workplaces. However, no documentation of that decision has been made public.

DOD Agencies Developing VI Guidance

While EPA is in the processing of putting the final touches to its revised VI guidance, we have learned that the Army, Navy and Army Corps of Engineers are all in the process of developing their own VI guidance. Both the Navy and Army declined to make them available for review. It appears that Corps guidance has been completed from a technical standpoint but its publication is being held up by the Office of Legal Counsel.

Commentary: *EPA's Office of Research and Development recently announced the availability of two useful reports that update current information available on the vapor intrusion pathway.*

The first report, "Review of Recent Research on Vapor Intrusion" indicates that the intrusion of contaminated vapors into buildings may provide a significant pathway for exposure to hazardous contaminants. The study stated that assessment of these problems is difficult because of limitations of sampling methodologies, contamination in ambient air, internal sources and sinks of contaminants and uncertainty in model application.

The second report "Uncertainty and the Johnson-Ettinger Model for Vapor Intrusion Calculations" evaluates the application of the Johnson-Ettinger Model for assessing the impact of contaminated vapors on residential indoor air quality. This analysis indicates that a simple one-at-a-time parameter uncertainty analysis provides a rough guide for the uncertainty generated by individual parameters. However, one-at-a-time analysis underestimated the uncertainty in the model when all or groups of parameters were assumed to be uncertain. According to this study, there was an apparent increase was as much as 1285% in simulated cancer risk caused by the uncertainty introduced from the input parameters.

EDR Launches Initiative to Help Companies Achieve FIN

47 Compliance

Environmental Data Resources, Inc. (EDR) recently announced that it had developed a product to help companies streamline the process for identifying and measuring conditional asset retirement obligations (CAROs) to ensure compliance with the new Financial Accounting Standards Board (FASB) interpretation of Statement 143 (FIN 47).

The new product is designed to assist companies with the first and perhaps most challenging step in the FIN 47 process--identifying asset retirement obligations that need to be accounted for on the balance sheet. EDR said companies will be able to use its environmental database to quickly assemble information on assets with environmentally sensitive operations such as UST and hazardous or solid waste management units that could have CAROs. Companies that have already inventoried their CAROs can use the EDR database to review the accuracy of their information. Once companies have identified their CAROs, they can then assess, measure and accurately report the impact of CAROs on their financial statements.

SIGNIFICANT LEGISLATION AFFECTING TRANSACTIONS

Roundup of Recent Aviall Cases

After the latest round of cases interpreting the Supreme Court's decision in *Cooper Industries v. Aviall Services*, 540 U.S. 1099 (2004), it appears that the best strategy for parties to recover their costs for voluntarily remediating sites is to argue that they have an implied right of contribution under section 107(a) of CERCLA.

In *ASARCO Inc. v. Union Pacific Railroad Co*., 2006 U.S.Dist. LEXIS 2626 (D. Ariz. 1/24/06), District Court for the District of Arizona ruled that a memorandum of agreement (MOA) entered into with a state environmental agency did not qualify as an administrative settlement under § 113(f)(3)(B) of CERCLA. As a result, the plaintiff was prohibited from bringing a contribution claim to recoup a portion of the $30 million in remediation costs it incurred. In this case, the plaintiff agreed to remediate a former lead smelter case pursuant to an MOA with the Nevada Department of Environmental Quality (NDEQ). In granting the defendant's motion for summary judgment, the court noted the MOA did not state that the plaintiff was resolving CERCLA liability or make any reference to CERCLA. In fact, the court observed, the only reference to federal law in the MOA was that the cleanup had to be consistent with the NCP. Instead, the agreement stated that the NDEQ was authorized to enter into the MOA pursuant to the state Remedial Action Plan Monitoring Act (RAPMA). The NDEQ also promised to issue a NFA letter under RAPMA after the plaintiff transferred title to the City of Omaha for use as a park or other open space. The plaintiff had pointed to the fact that EPA had reviewed and approved a remedial action workplan (RAWP). However, court said that the plaintiff was not required to submit the RAWP to EPA, that the federal agency had stated in a letter that it was simply providing technical assistance to NDEQ, and that EPA indicated that NDEQ was the lead agency for the remedial action.

In re FV Steel & Wire Co., 331 B.R. 385 ((Bankr. E.D. Wis., 2005), the debtor withdrew from a participation agreement entered into with other PRPs to remediate a site and filed for bankruptcy. After the debtor withdrew from the agreement. EPA issued an administrative order for additional work. The PRPs filed proofs of claim in the bankruptcy proceeding. The bankruptcy court ruled that the administrative order did not quality as a civil action under §113(f)(1) and that the Seventh Circuit had rejected the concept of an implied right of contribution under §107. As a result, the court ruled that the PRPs claim should be disallowed.

In one of the few victories for voluntary remediators, the district court for the northern district of

California permitted plaintiffs to proceed with a contribution action brought under §107(a) of CERCLA. In *Aggio v. Estate of Aggio***,** 2005 U.S. Dist. LEXIS 37428 (N.D. Cal., Sept. 19, 2005), Joseph Aggio owned a 156-acre parcel of real property in Cotati, CA from 1947 until his death in 1988. The ownership of the property then passed to his widow and their three sons when the widow died in 1989. The Aggio brothers sold the property to the Marvin K. Soiland Family Trust in 1998. From 1958 to 1996, Cotati Rod & Gun Club ("CRGC") leased ten acres of the site to operate trap and target ranges, which resulted in the deposit of lead shot, clay target waste, and other materials at the property. After CRGC filed for bankruptcy protection, plaintiffs entered into a voluntary cleanup agreement with the California Department of Toxic Substances and Control. Plaintiffs filed a contribution action under CERCLA § 113(f) 2004 against CRGC, the Marvin K. Soiland Family Trust and the insurer of the estate of their father, Sequoia. After the plaintiffs settled their claims against the CRGC and the Marvin K. Soiland Family Trust, the Supreme Court handed down its *Aviall* ruling. Following *Aviall*, the plaintiffs filed an amended complaint to add a cost recovery claim under CERCLA § 107(a). Sequoia then filed a motion to dismiss, arguing that the plaintiffs were not entitled to assert a §107 contribution claim. The district court noted that there had been four post-*Aviall* decisions in the Ninth Circuit. In *Koutrous v. Goss-Jewett Co. of Northern Cal., Inc*., 2005 WL 1417152 (E.D. Cal., June 16, 2005); *Adobe Lumber, Inc. v. Taecker*, 2005 WL 1367065 (E.D. Cal., May 24, 2005) and *Ferguson v. Arcata Redwood Co., LLC,* 2005 WL 1869445 (N.D. Cal., Aug. 5, 2005) the courts found that there was an implied right of contribution under § 107(a). The court found the analysis in those three cases better than the one decision that ruled that there was no such implied right of contribution, *City of Rialto v. U.S. Department of Defense,* 2005 U.S. Dist. LEXIS 26941 (C.D. Cal., August 16, 2005).

In contrast to *Aggio* was the district court for the eastern district of California in *Adobe Lumber, Inc. v. Hellman*, 2006 U.S. Dist. LEXIS 136 (January 6, 2006) where a shopping center current owner sought to recover its costs to remediate contamination associated with dry cleaning tenant. The court found that the dry cleaners, city, manufacturers, and that the prior owners made a plausible argument that the current owner had no PRP right to contribution for voluntarily incurred clean up costs under § 107(a). However, because the issue of the implied right of contribution under §107 had been appealed to the Ninth Circuit, the court denied their motion to dismiss and postponed discovery until the Ninth Circuit resolved the issue.

Finally, the City of Waukesha is nothing if not persistent. Last spring, a federal district court ruled that a cost share agreement that the city had entered into with the Wisconsin Department of Natural Resources (WDNR) did not qualify as an administrative settlement and therefore it was not entitled it to bring

a §113(f)(3) contribution action. Not to be rebuffed, the city subsequently entered into an agreement with the WDNR that was captioned as a settlement agreement and specifically provided it resolved the potential claims that the WDNR might have against the city under CERCLA. The city then filed a motion to amend its complaint to add a contribution claim under §113(f)(3). Once again, though, the city was denied. *City of Waukesha v. Viacom International, Inc.*, 404 F.Supp.2d 1112 (E.D.Wis. 2005) Pointing to the reservation of rights clause, the court said that the city had not settled its CERCLA liability since the WDNR retained the right to sue under CERCLA if the city did not satisfactorily perform its obligations. The court observed that the agreement did not refer to the NCP but instead required the city to comply with the Wisconsin Administrative Code.

In concluding its analysis, the court said the best evidence to support its conclusion that the city had not resolved its CERCLA liability was that the WDNR had not been authorized to administer CERCLA under §104(d)(1)(A) despite the fact that WDNR had entered into a number of ongoing cooperative agreements with EPA. This included a 1990 agreement where EPA specifically tasked WDNR to conduct site screening activities at the very landfill that was the subject of the litigation. In the absence of an express provision stating that the WDNR was entering into the agreement on behalf of the federal government and the fact that EPA had not waived its rights under CERCLA, the court held that the city had not resolved its CERCLA liability and denied the motion to amend its complaint.

Commentary: *In holding that the state agreements were not administrative settlements under §113(f)(3), the Asarco and Waukesha cases relied heavily on the fact that the states had not been authorized under §104(d)(1)(A) of CERCLA to enter into CERCLA settlements. The reliance on this section appears to be misplaced. In the early days of the CERCLA program, some states without robust state cleanup programs entered into cooperative agreements with EPA to allow sites to be remediated under the state program and defer having the site listed on the NPL. However, this arrangement has rarely been used since the mid-1980s. Because developers who remediated sites under a state program wanted some assurance that they would not find themselves subject to additional cleanup demands from EPA, the agency began entering into memorandums of understanding (MOUs) with state environmental agencies. EPA agreed it would not require additional work so long as the remediation was performed in accordance with the state requirements. The 2002 CERCLA amendments codified this approach when a new §128 was added that provided for a federal enforcement bar if a site was remediated pursuant to a state program that was either subject to a MOU or that qualified as "state response programs." Due to §128, courts should not use the absence of a cooperative agreement under §104(d)(1)(A) as a basis for*

determining that an agreement with a state environmental agency is not a settlement agreement within the meaning of §113(f)(3).

New York Files Cost Recovery Action Against Holder of Mortgage Note

In *State of New York v. Fumex Sanitation* et al, No. CV04-1295 (E.D.N.Y), the NYSDEC has filed a CERCLA cost recovery action seeking reimbursement of $500,000 in past response costs from the owner and operator of the Fumex Sanitation site as well as the purchaser of a mortgage note. The state is also demanding that the parties implement a remedy that is estimated to cost $628,000 and seeking natural resources damages.

In this case, Fumex Sanitation, Inc., (Fumex) entered into an administrative order with the NYSDEC in 1986 to investigate the extent chlordane contamination resulting from a 1981 spill at its facility in Hempstead, New York. In 1989, Roosevelt Savings Bank (Roosevelt) made a $240,000 loan to Fumex that was secured by a mortgage on the Fumex property. Around this time, NYSDEC commenced another investigation and listed the facility as a class 2 site on the registry of state superfund sites. In 1991, Fumex defaulted on the note and Roosevelt commenced foreclosure proceedings though it appears that Roosevelt never actually took title. After Fumex refused to take any further actions at the site, NYSDEC implemented an RI/FS. In 2000, Roslyn Savings Bank, the successor to Roosevelt, assigned the mortgage note to Dynasty Products. NYSDEC then issued a ROD in March 2001.

Discovery has not yet commenced in this case. However, based on the pleadings and conversations with counsel, it appears that the plaintiff is alleging that the purchaser of the note is not entitled to the secured creditor exemption because it exercised decision-making control over the property by participating in negotiations with the NYSDEC and repairing the roof. It also appears that the state is claiming that the note holder assumed responsibility for management of the site by collecting rent from tenants and paying real estate taxes.

Commentary: *The CERCLA secured creditor exemption provides that a lender who holds indicia of ownership primarily to protect its security interest will not be considered an owner of a property if it does not participate in the day-to-day environmental management of the facility. If the secured creditor forecloses on the property, it may still maintain its liability exemption so long as it takes steps to sell the property in a commercially reasonable manner.*

In this case, the state is arguing that the purchaser of the note is an owner under CERCLA because it has participated in the management of the property. However, the facts that the state has thus far relied upon appear to be insufficient to impose CERLA owner liability on the note holder. The overwhelming weight of authority interpreting the secured creditor exemption and EPA's 1992 lender liability rule that Congress codified in

1996 with the lender liability amendments to CERCLA clearly state that lenders will not lose their immunity from liability so long as they take steps that are consistent with prudent lending practices and protection of its security interest. Collecting rent, paying taxes and even repairing the roof would appear to be the kind of actions that a lender would do to protect its collateral value.

If the primary motive of the purchaser of the mortgage note was not to protect its security interest but to protect an investment interest in the property, then the note holder would not be entitled to CERCLA's safe harbor for secured creditors. However, thus far, the state has not pleaded that point.

Existence of REC Allows Purchaser to Postpone Closing

In *Munter v. 365 Glen Cove Realty, LLC*, No. 2126/05 (Nassau Sup. Ct. 9/9/2005), the plaintiffs entered into a contract to purchase commercial property for $610,000 on October 12, 2004. The contract had a mortgage contingency and provided that the seller would deliver the premises free of all encumbrances at the closing scheduled for November 29, 2004.

On November 18th, HSBC Bank issued a mortgage commitment that was subject to an acceptable Phase I environmental site assessment. The environmental report was not completed by the closing date and seller's counsel notified plaintiff that the mortgage contingency was cancelled and that a time of essence closing was scheduled for January 7, 2005. However, the Phase I ESA report issued on December 21st identified a former fueling facility on the property as a REC, and recommended that a Phase II ESA be performed. The Seller refused to allow any sampling. The closing did not take place and plaintiff notified defendant that it was terminating the contract and demanded return of its down payment. When seller refused, plaintiff commenced its action.

The court granted plaintiff's motion for summary judgment. The court found that the defendant acted in bad faith when it failed to allow the plaintiff to comply with its mortgage contingency by performing a Phase II ESA. The court also ruled that the existence of a REC was an encumbrance because it can lower the value of the property. Since the seller failed to deliver the premises free from any encumbrances, the court held that the seller was unable to fulfill its obligations under the contract and plaintiff was entitled to its down payment.

Ohio Court Rules that Cost of Phase I Required by Lender Not Recoverable

In *Weber v. Obuch,* 2005 Ohio App. LEXIS 6314 (Ct. App.-9th Dist. 12/30/05), the plaintiff purchased an undeveloped parcel of land in 1997 for $40,000 that was located next to a gasoline station. In 2000, plaintiff decided to construct a building and was required to perform a Phase I ESA as a condition of the construction loan. When the Phase I ESA identified contamination associated with adjacent gas station, the bank required a Phase II ESA,

which estimated the cleanup costs at $15,000. Plaintiff then commenced its lawsuit seeking recovery of its costs and damages of future rental income. The trial court awarded damages to the plaintiff but appealed the amount of the damages.

The appellate court held that the plaintiff was not entitled to recover the costs of the Phase I ESA because the report was required by the lender and not related to the contamination. However, because the Phase II ESA was required because of the evidence of the contamination, the plaintiff was awarded the costs of the Phase II ESA.

On its property damage claim, the court found that the loss of use claim was too speculative since the property was vacant. However, on the claim for diminution in property value, the court found that the plaintiff had established that the property would be worth $80,000 in a remediated state, but was only worth $40,000 in its contaminated state. Thus, the court remanded this issue back to the trial court for a proper determination of the property damages.

Landlord Allowed To Recover Damages After NFA Letter Reopened

In *General Dynamics Corporation v. Paulucci*, 2005 Fla. App. LEXIS 18243 (Ct. App.-5th Dist. 11/18/05), landlord Paulucci filed a complaint in 1996 alleging that General Dynamics Corporation (GDC) had contaminated the warehouse that GDC had leased. In February 1997, the Florida Department of Environmental Protection (DEP) issued a NFA letter based on sampling from two wells.

In May 1998, though, contamination was detected on another portion of the property. Two months later, the parties reached a settlement where GDC agreed to pay $3 million and promptly contacted the Florida DEP to maintain the NFA or obtain reissuance of the NFA. The settlement also provided that if the a valid NFA letter was not in place after 15 months of the date of the settlement agreement, GDC would be required to make monthly rental payments until a valid NFA was in effect.

GDC did not promptly disclose the results of the 1998 report to the Florida DEP. The landlord obtained a court order requiring GDC to notify the agency, which required additional remediation. A new NFA was not issued until March 2002. The landlord then sought to enforce the stipulated damages provision.

GDC argued it was not liable for the payments because the DEP had never withdrawn the NFA. However, DEP employees testified that the 1997 NFA was based on the information provided to the agency and once it discovered contamination elsewhere at the property, the 1997 NFA was no longer valid for the rest of the property. Since the Florida DEP required further action, the court ruled that the landlord was entitled to the stipulated damages.

Commentary: *This case illustrates the importance of determining the scope of an NFA letter. As we discussed in our vapor intrusion coverage, agencies will issue NFA or*

closure letters based on the information that was provided. The NFA determinations usually have reopeners allowing the agency to require additional work under certain circumstances. During due diligence it is important to determine what information was provided to the agency, if the NFA applied to the entire site or just a portion of the site and also to determine if there are any institutional or engineering controls that must be maintained to preserve the validity of the NFA letter.

Court Awards Damages To Adjacent Landowner Despite NFA Letter

In *Ronald Holland's A-Plus Transmission & Automotive, Inc. v. E-Z Mart Stores, Inc.,* et al 2005 Tex. App. LEXIS 9875 (Ct. App- San Antonio 11/30/05), the defendant obtained closure from the predecessor of the Texas Natural Resources Conservation Commission (TNRCC) in connection with the removal of leaking USTs.

In May 2001, the plaintiff agreed to lease a portion of his farmland to Trinity Wireless who planned to erect a cell tower. An explosion occurred while Trinity was boring a hole for the cell tower. Soil sampling was conducted and found benzene levels at eight times the TNRCC action level. By 2004, the benzene levels were 34 times the action level. Trinity's consultant determined that gasoline had migrated from the E-Z Mart store and Trinity terminated its lease.

The plaintiff sought damages for negligence, trespass and nuisance. The defendants argued that the plaintiff was barred as a matter of law because of the TNRCC closure letter. The trial court agreed, but the appeals court reversed and remanded the case to the trial court for further proceedings.

The court said that to maintain an action when a cleanup has already been performed, a plaintiff must show that there were "unreasonable levels" of contaminants (*i.e.,* contamination above state action levels). The court also said that if unreasonable levels of contamination were subsequently discovered, the site closure letter would not exonerate the liability of the discharger. The defendants argued that the plaintiff had not established that there were any actionable levels of contaminants on the E-Z Mart site. However, the court found that the plaintiffs had produced sufficient evidence to show that the actionable contamination on its property was from the E-Z Mart site. The plaintiff also introduced evidence showing that there had been a gap in the groundwater wells on the E-Z Mart site that had missed the portion of the plume that was migrating onto the plaintiff's property.

Because the groundwater on the plaintiff's property contained MTBE, the court ruled that the plaintiff could not recover from one defendant who had operated the gas station in the 1980s before gasoline with MTBE was sold.

Owner Who Knowingly Acquired Contaminated Property Allowed to Assert Innocent Purchaser Defense

A city that knowingly acquired title to contaminated property was

allowed to pursue a claim for CERCLA § 107 cost recovery action in *City of Mishawaka v. Uniroyal Holding Inc.,* 2006 U.S. Dist. LEXIS 4372 (N.D. Ind. 1/19/06). In 1997, EPA incurred $1.5 million in emergency response costs at a manufacturing facility that had been owned by a predecessor of the defendant. After EPA completed its removal action, the city acquired a leasehold interest with an option to purchase the former manufacturing facility. In 1999, the city entered into a prospective purchaser agreement (PPA) with EPA and exercised its option to purchase. The PPA obligated the city to assess and remove asbestos-containing materials, but the city performed additional remedial activities not required by the PPA. At the same time, the defendant negotiated a covenant not to sue in exchange for a payment of $100,000 that provided contribution protection to the defendant. After the city filed its cost recovery action, the defendant moved for summary judgment, arguing that the city was a PRP that was only permitted to bring a contribution action, and that the action was barred by the settlement the defendant had reached with EPA.

The court rejected the city's assertion that it was an innocent landowner by virtue of the PPA. However, the court ruled that since the hazardous substances were disposed at the site prior to the time that the city acquired title, it was considered a "non-polluting" PRP that the Seventh Circuit had recognized as qualifying for as innocent purchaser. Thus, the court held that the city could pursue a cost recovery action, and was not barred either by the contribution bar contained in the defendant's settlement with EPA or *Aviall.*

Commentary: *Since the property was acquired prior to January 11, 2002, the city was not entitled to assert the bona fide prospective purchaser defense. Thus, it was limited to either the innocent landowner or third party defenses. Both of these defenses are affirmative defenses, which means that the city should have had the burden to establish by a preponderance of the evidence that it satisfied the elements of these defenses. The city clearly knew the property was contaminated so it should have been entitled to assert the innocent purchaser defense. Because the case is devoid of any analysis, it is unclear if the city would have qualified for the third party defense. Instead, the court focused its opinion on a quirky rule adopted by the Seventh Circuit that a property owner who does not actually cause the contamination is not a potentially responsible party under CERCLA. Since the city took title after the contamination, presumably the court felt the city was exempt from liability and did not have to assert any defenses to liability. Thus, this case should only serve as precedent in states that are located in the Seventh Circuit.*

Property Owner Who Failed to Perform Recommended Phase II ESA Prohibited From Recovering Past Costs

In *50 Day Street Associates Limited Partnership v. Norwalk*

Housing Authority, 2006 Conn. Super. LEXIS 223 (2005), the plaintiff investors purchased a commercial property in 1984 without performing a Phase I ESA investigation. When the plaintiffs decided to refinance in 1999, their lender required a Phase I ESA and limited subsurface investigation. When the Phase II ESA revealed the presence of petroleum contamination, the bank declined to refinance the property. The plaintiff subsequently determined that the likely source of the contamination was three heating oil tanks located at housing complex owned by the Norwalk Housing Authority. Two of the heating oil USTs had been installed in 1976 and one had been put into service in 1941. NHA conducted its own investigation and concluded that while the soil around the USTs was impacted, the petroleum was not the same that was detected in the groundwater at the plaintiff's property. Nevertheless, NHA subsequently removed the three USTs and the oldest tank was observed to have numerous holes.

The plaintiffs sought damages under statutory and common-law claims. The court concluded that NHA was negligent for continuing to use the USTs beyond their useful life and unreasonably delaying removing the tanks for almost two years. However, the Court concluded that the plaintiffs had not proved that the source of the contamination was the NHA property because of questions about the groundwater flow direction.

The court then went on to hold that the plaintiffs were entitled to damages under the Connecticut Environmental Protection Act (CEPA). Under this law, an action may be maintained against any person whose acts cause "unreasonable pollution, impairment or destruction" of natural resources of the state. The court noted that the Connecticut Supreme Court defined "unreasonable" pollution to be pollution that is not in compliance with the regulatory and legislative scheme established by CEPA. Since the NHA's leaking USTs caused soil and groundwater in excess of the state cleanup standards, the Court ordered NHA to remediate its property and pay for some of plaintiff's attorneys' fees.

The plaintiff moved for reconsideration to submit groundwater data collected after the trial that suggested groundwater did flow from NHA's site across plaintiff's property. The court noted that the standard for admitting "newly discovered" evidence is that it could not have been discovered earlier by the exercise of due diligence and that it was likely to produce a different result in a new trial. The court refused to admit this information because the plaintiff had failed to follow the recommendation of its consultant in 2001 to install groundwater wells on both parcels because the consultant that it believed the NHA site was upgradient to the plaintiff's property. Since there was some question if the current groundwater flow was influenced by the recent treatment system and because plaintiff did not have groundwater data from around the time when the release occurred or was migrating, the court also felt that the information was not likely to affect the outcome of the case. Accordingly, the plaintiff's motion was denied.

SUPERFUND/BROWNFIELDS

EPA Announces PPA Settlement

Proposed prospective purchaser agreements (PPAs) have become the endangered species of the CERCLA. Once in awhile, though, EPA will enter into an agreement for projects sponsored or strongly supported by local government. The latest PPA sighting involved a property located in East Farmingdale, NY. Under this agreement, EPA and the State of New York agreed to provide a covenant not to sue to Suffolk County and an as-of-yet unnamed "Auction Purchaser" for a 0.9-acre parcel located within the Circuitron Corporation Superfund Site. Suffolk County agreed to market the property at auction with a portion of the proceeds to be paid to EPA for reimbursement of past response costs. EPA also agrees to release its CERCLA Section 107(l) lien and waive any windfall lien or right to perfect any windfall lien that it may have now and in the future

EPA also announced that it had agreed to enter into a PPA with Phoenix International Terminal, LLC ("Phoenix") to facilitate the acquisition of 140 acres of property known as the Operable Unit Number One of the Tex Tin Corporation Superfund Site. Phoenix intends to use the property to construct Phoenix plans to use the site to build freight and storage facilities to support Texas City deep-water terminal at Shoal Point, now under construction, approximately 1.5 miles from the Site. This site, which is currently owned by the Tex Tin Site Custodial Trust, was one of the first NPL sites to receive a ready for reuse (RfR) certificate. In exchange for a Covenant Not to Sue for the existing contamination at the Site, Phoenix agreed to pay $1,000,000 to the Trustee of the Tex Tin Custodial Trust. The Trustee will pay any outstanding liens on the property and any other expenses required by the Custodial Trust Agreement, and pay the balance of the purchase price left after payment of Trust expenses to EPA. In addition, Phoenix agreed to provide an irrevocable right of access to EPA.

DTSC Obtains Court Order To Impose Deed Restrictions

What do you do if you need to file a deed restriction on a property as part of a remedial action, but the owner is deceased? If you are the California Department of Toxic Substances Control (DTSC), you get a court order.

In *State of California v. Agajanian,* No. CVF96-5176 (E.D.Cal. 12/19/05), the DTSC issued an Imminent and Substantial Endangerment Order to the owner of the Silver Queen junkyard in 1997. When the owner failed to comply with the order, the DTSC performed a removal action and then obtained a declaratory judgment finding the owner liable under CERCLA for the state's past costs and an injunction requiring the owner to complete the cleanup. When the owner advised

that DTSC that he was financially unable to implement the remedy, the agency implemented its remedial action plan for the site. The remedy included a deed restriction limiting the property to industrial or commercial use as well as maintenance of a concrete cap. The DSTC intended to place a deed restriction on the site with the permission of the owner. However, the owner passed away in 2000 and title was held by the "Agajanian Trust." The DSTC searched the county probate records in the three counties where the defendant had lived or owned property but failed to find any person or entity acting as executor of the trust, or for that matter any probate records. The agency then conducted a property search to locate the addresses for potential relatives of the defendant and sent correspondence to several relatives, but either received no response or the individuals indicated that they were not involved with the trust or the defendant. As a result, the court issued an "Order Restricting Use of Property" and the DSTC recorded the order in the Kern County Recorder's Office.

Commentary: *Since groundwater plumes do not recognize property boundaries, responsible parties are increasingly having to obtain institutional controls (ICs) on properties adjacent to a contaminated site. ICs impose use restrictions, usually in the form of prohibitions on using the groundwater, but sometimes on limiting the use of property. Not surprisingly, property owners are frequently reluctant to agree to such prohibitions or insist on some form of compensation.*

Remediators who encounter resistance from such adjacent property owners may want to consider reminding them of their obligations under CERCLA if the downgradient or adjacent landowner wants to maintain its liability protection. Under the 2002 amendments to CERCLA¸ if the property owner wants to maintain its CERCLA liability exemption as a contiguous property owner, it must cooperate and provide access to persons responsible for implementing remedial actions and also comply with institutional controls.

If the site is being remediated under a state response program that does not have a policy or statutory defense for downgradient property owners, it may be possible to have the state agency issue a cooperation order to a reluctant property owner.

Availability of Federal Brownfield Grant Encourages Town to Exercise Its Power Of Eminent Domain

The Town of Hempstead recently obtained an order from a state court to take possession of parcel of land pursuant to the state Eminent Domain Procedures Law. *In the Matter of the Town of Hempstead Acquiring Property in the Urban Renewal Area Known as Jamaica Square, Elmont, New York as part of the Town's Federally Funded Community Development Program*, Index No. 00-13988 (Nassau Cty. Sup Ct. 09/15/05). The town advised the court that the

NYSDEC was willing to perform a Phase II ESA on the property pursuant to a federal brownfield grant and that the town would prefer to use the grant money so that its taxpayers would not have to pay for the investigation.

This matter began back in 2001 when the town acquired title to a site owned by Bob's Crown Welding. The court indicated that the town was entitled to perform a full environmental investigation on the property as part of the condemnation proceeding to determine if an offset to the acquisition price. In March 2002, the town agreed to make an advance payment of $192,000 for an automobile repair and welding shop, which exceeded the appraisal by approximately $30,000. The town issued a thirty-day notice to vacate in October 2002, but the property owner refused to vacate the premises, arguing that the advance payment was insufficient.

In its application for the order to vacate, the town indicated that a Phase II ESA performed on the adjacent property established that the two properties were significantly contaminated and that the Phase II ESA on the welding shop property could not be performed until the owner of the shop removed his heavy equipment and personal property from the site.

The court found that further delay would prejudice the town and ordered that it be awarded immediate possession of the premises and authorized the sheriff to remove all personal property and equipment located on the property. Finally, the court ordered that the balance of the condemnation award be held in escrow pending a determination of the estimated cleanup costs. A separate proceeding would be held to determine the condemnee's responsibility for the remediation costs related to the property.

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