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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.

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LITIGATION IMPACTING TRANSACTIONS

FINALLY! A Post-Aviall Decision that Makes Sense

In our last issue, we chastised a number of federal district court decisions that had relied on an obscure provision of CERCLA to rule that state cleanup agreements did not qualify as administrative settlements for purposes of bringing a contribution action under section 113(f)(3) of CERCLA. We would like to think that the District Court for the Western District was influenced by our criticism of those decisions when it ruled that the plaintiff could bring a contribution action in *Seneca Meadows, Inc. v. ECI Liquidating, Inc., 2006 U.S. Dist. LEXIS 21507* (W.D.N.Y. April 20, 2006). More likely, though, it was probably the *amicus* brief filed by the New York State Department of Environment Conservation (NYSDEC) that convinced the court to refuse to follow the bizarre reasoning of those cases.

In this case, the Seneca Meadows, Inc. (SMI) acquired a landfill that had been operated for thirty years and closed in 1974. The plaintiff then obtained a permit to expand a portion of the landfill in 1981. Two years later, NYSDEC listed the site as a class 2 Inactive Hazardous Waste Disposal Site, which is the New York equivalent to a federal NPL site. The plaintiff entered into three orders on consent with the NYSDEC to remediate a closed landfill and had incurred approximately $8 million in response costs by March 2005 and anticipates that the final response costs would be around $16 million. All of the consent orders were executed prior to the United State Supreme Court's decision in *Cooper Industries v. Aviall Services, Inc*., 543 U.S. 157 (2004)(Aviall). The three NYSDEC consent orders referred to CERCLA and provided SMI with contribution protection under §113(f)(2) of CERCLA.

SMI filed contribution claims against generators who had disposed of industrial wastes at the 26-acre site and had settled with all but one of the defendants, Goulds Pumps, Inc. (Goulds). Citing the *W.R. Grace & Co. v. Zotos Int'l, Inc*. (2005 WL 1076117) decision issued by another judge in the same district, Goulds argued that the NYSDEC could not resolve SMI's CERCLA liability because EPA had never delegated CERCLA settlement authority to NYSDEC. The court acknowledged that NYSDEC had not entered into a cooperative agreement pursuant to §104(d)(1). However, the court said that while a state may not act on behalf of the federal government without delegation from EPA, §104(d)(1) did not prohibit states from using their own resources to remediate releases of hazardous substances and seeking to recover their costs from responsible parties under state law or CERCLA.

Even if the consent orders were not administrative settlements for purposes of §113(f)(3), the court held that SMI could bring a contribution action under §107. Gould argued that the Second Circuit had previously ruled in *Bedford Affiliates v. Sills*, 156 F.3d 416 (2nd Cir. 1998) and *Consolidated Edison Co. v.UGI Utilities, Inc*, 423 F.3d 90 (2d Cir. 2005) that only innocent parties could maintain §107 actions against potentially responsible parties. However, the court said that *Bedford* was of dubious validity following *Aviall*. In light of CERCLA's purpose to encourage prompt cleanups and the absence of clear language in the statute, the court said the Bedford holding should not be applied in a simplistic and mechanical fashion.

The court said that the key factor distinguishing Bedford from the instant case was the distinction between a cost recovery action where the plaintiff seeks indemnity or full recovery of its costs and a contribution action where the plaintiff is seeking to recoup only those costs that exceed its fair share of the total costs. The concern of the Bedford panel, the court explained, was that the plaintiff was seeking 100% of its costs and not simply those costs that exceeded its equitable costs. Likewise, the court said Con Ed involved a party that incurred response costs voluntarily whereas SMI had incurred the costs pursuant to a consent order.

Finally, the court found that the plain language of the consent orders showed SMI and NYSDEC clearly intended for SMI to enjoy contribution protection under §113(f)(2) and expressly reserved the right for SMI to seek contribution under §113(f)(3). It would be inequitable and inconsistent with the purpose of CERCLA as had been articulated by the Second Circuit in the past, the court reasoned, to allow what was at worst a technical omission that only took on significance after the Aviall decision to bar SMI from seeking contribution.

Commentary: *In the wake of Aviall, courts are beginning to find ways to distinguish prior decisions ruling that responsible parties may not seek reimbursement of their costs under §107.*

One of the first cases to interpret the Aviall decision was AMW Materials Testing Inc. v. Town of Babylon, 348 F.Supp.2d 4 (E.D.N.Y. 2004) where a federal district court dismissed the CERCLA and common law claims against the local fire department. On appeal, the Second Circuit affirmed the dismissal of the §113(f)(1) but vacated and remanded the ruling that the plaintiff could not bring a contribution action under §107 (2006 U.S. App. LEXIS 8545, March 28, 2006).

In McDonald v. Sun Oil Company, 2006 U.S. Dist. LEXIS 14725 (D.Or. March 14, 2006), the district court for the district of Oregon ruled that that a responsible party that voluntarily remediates its property could bring a §107 contribution action. In this case, plaintiffs acquired property that had been previously used for mining mercury and contained calcine tailings. In 2001, the Oregon Department of Environmental Quality (DEQ) determined that the plaintiffs handling of the tailings had created

releases and ordered them to refrain from removing or disturbing the tailings without DEQ approval. The court found that the plaintiffs did not qualify for the innocent purchase defense because they were aware of the presence of the mercury-contaminated tailings and could not assert the third party defense because they failed to exercise due care regarding the tailings. Although the plaintiffs were considered responsible parties, the court said that they could bring a §107 contribution action under Ninth Circuit precedent.

Class Action Claim Against Fiduciary Bank Dismissed

A putative class action filed against officers and directors of Solutia, Inc., and the fiduciary of the employee savings plan brought by a former Solutia employee on behalf of the Solutia Savings and Investment Plan (Plan) was dismissed by a federal district court in *Dickerson v. Feldman,* 2006 U.S. Dist. LEXIS 14230 (S.D.N.Y. March 30, 2006).

In September 1997, Monsanto Company spun off its chemical business and formed an independent company, Solutia, Inc. The plaintiff alleged that Monsanto created Solutia to unburden itself of substantial and undisclosed environmental liabilities. They allege that the officers and directors knew Solutia did not have adequate capital to cover its liabilities yet caused the Plan to continue to invest in Solutia stock. Moreover, the plaintiff asserted that the Plan administrator, Northern Trust Company, continued to follow the investment instructions without inquiry and despite publicly available information that should have raised questions about the ability of Solutia to remain a viable company.

The plaintiff had left the company in 2003 taking a full distribution of his benefits from the Plan before commencing the lawsuit. Since the plaintiff no longer had a vested interest in the Plan and did not allege that he was misled into taking a full payout of his vested benefits or was influenced in any way by Solutia to do so, the court ruled that the plaintiff had no standing to bring the action and dismissed the lawsuit.

***Commentary**: This case was dismissed on procedural grounds so the court did not have an opportunity to evaluate the merits of the plaintiff's claims. However, it is not uncommon for companies undergoing restructuring to place environmentally distressed properties into separate legacy corporations whose only assets are the contaminated properties. This lawsuit may serve as a shot across the bow to companies and their professional service providers or advisors that this strategy may not be without considerable risk.*

Landowner Awarded Damages for Contaminated Fill Material

In *Hall v. Hubco*, 2006 Tex. App. LEXIS 1037 (Ct. App. February 9, 2006), the administrator of an estate that owned land with a partially excavated pit arranged with the defendant in November 1998 to dump excess "clean fill" to bring the property up to grade and increase its

marketability. The contractor also agreed to grade and survey the property.

In February 1999, the administrator visited the property and observed a black, tar-like substance emanating from the soil. Soil sampling subsequently confirmed the soil was contaminated and demanded the defendant remove the contaminated fill. The defendant denied he had disposed contaminated soil, but agreed to remove the soil "as a favor." The parties entered into a handwritten agreement in June 1999 whereby the defendant agreed to remove the "tar-like substance," replace it with clean fill and properly dispose of the waste material. The defendant removed the contaminated soil, but failed to properly dispose of it and left it stockpiled on the property.

The plaintiff then filed a breach of contract action. After a jury trial, the plaintiff was awarded approximately $107K to dispose of the contaminated soil, $2K for the cost of the fill material, $8K for failing to grade and survey the property, $165K in damages for diminished property value and approximately $45K in attorney fees. However, the trial court disregarded several of the jury's damage awards. First, the court ruled that the June contract was not enforceable because there was no consideration for the agreement. In addition, since the plaintiff's expert had based the disposal costs on two samples and admitted he could not accurately estimate the total disposal costs without further sampling, the court ruled the testimony for disposal costs was unreliable and could not serve as evidence for the jury to use. As a result, the court reduced the verdict to $10K plus attorneys' fees. Both parties appealed the decision. The appeals court affirmed the disallowing of the disposal costs and the $2K award for the breach of the June agreement. However, the court affirmed the rest of the damages.

Court Clarifies Who May Enforce CT Transfer Act

The Connecticut Transfer Act (CTA) requires transferors of "establishments" to provide one of four types of disclosure forms to a purchaser. A transferor who fails to comply with the CTA is strictly liable for all remediation costs as well as direct and indirect damages suffered by "a transferee." A question that has periodically surfaced is whether a seller may be strictly liable to subsequent property owners who do not have a contractual relationship with the seller. In an unreported decision, a state court ruled in *East Greyrock, LLC v. OBC Associates*, 2006 Conn. Super. LEXIS 383 (Ct.Sup. February 7, 2006) that the transferor may only be liable to its direct transferee for failing to comply with the CTA.

In this case, Oysterbend Properties was sold to one of the defendants, Richard Scalise, in 1983. The property was formerly a barrel and reconditioning facility and a construction equipment storage yard. The facility was placed on the federal CERCLIS in 1984 and the state list of hazardous waste sites in 1987. In 1988, approximately 22,000 cubic yards of material dredged from the Norwalk River were deposited on the property.

In 1988, Scalise transferred the property to defendants R&G Industries and OBC Associates, Inc., without complying with the CTA. In 2002, the defendants sold their interest in Oysterbend Properties. The plaintiffs allege that the public offering statement failed to disclose the CERCLIS and state hazardous waste listing or that hazardous waste had been stored, disposed or released at the Property. The plaintiffs also asserted that Scalise as agent for the defendants, stated that all environmental investigations and remediation had been completed. Since the plaintiffs were not a party to the 1988 transaction that triggered the CTA, the court granted the defendants' motion to strike the CTA cause of action.

Commentary: *When there is a subsequent transaction involving a site that is being remediated under the CTA, the new purchaser will frequently require the prior seller to agree to execute new CTA forms as a "certifying party," reaffirming its responsibility for completing the cleanup.*

Broker Not Entitled to Fee Because of Contamination

A real estate broker is generally entitled to a commission when it has produced a ready, willing and able purchaser who came to a meeting of the minds with the seller on all material terms of the sale. Is a broker entitled to its commission when a buyer withdraws an offer to purchase property after learning that the seller failed to disclose the existence of contamination?

In *Heelan Realty and Development Corp. v. Ocskasy*, 2006 N.Y. App. Div. LEXIS 3484, a broker sought to recover a $13,300 real estate brokerage commission alleging that it had entered into a listing agreement with the defendant and had produced a prospective purchaser. The buyer withdrew its purchase offer after the after learning the property was contaminated and regulatory closure had not been obtained.

During the trial, the principal of the prospective buyer testified that it had not been advised of the presence of contamination, that the cleanup had not been completed, and that he could not state if the purchaser would have consummated the transaction if it had known of the contamination. As a result, the trial court said it was unable to conclude that a sale would have occurred based on the offer procured by the plaintiff. However, the court invoked its equitable jurisdiction and awarded the one-half of the commission sought by the plaintiff as compensation for its marketing efforts. The appeals court, though, reversed the lower court and dismissed the complaint on grounds that there was no basis for equitable relief.

Purchaser of Assets Pursuant to Bankruptcy Sale Liable for Pre-Existing Contamination

A recent trend in bankruptcy cases has been the sale of assets "free and clear" of interests and liens pursuant to section 363 of the Bankruptcy Code (Code) instead of through an approved plan of reorganization. Often times, the court

order approving the sales, may specifically provide that the purchaser is acquiring the assets free of any successor liability.

As illustrated by a recent federal court decision, a section 363 sale may not necessarily insulate a buyer from its ongoing environmental obligations associated with pre-existing contamination. In *U.S. v. Timmons Corp*., 2006 U.S. Dist. LEXIS 7642 (N.D.N.Y. February 8, 2006), the defendant purchased 163 acres that included a former steel foundry containing several transformers from the bankruptcy estate of the Adirondack Steel Casting Company, Inc. Prior to taking title, Timmons ordered a Phase I environmental site assessment that indicated that the transformers contained dielectric fluids with PCBs and that there were "hot spots" of stained concrete around several of the transformers.

In 1992, the New York Department of Environmental Conservation (NYSDEC) identified areas of soil with levels of PCBs as high as 299 ppm and of at least 3,000 gallons of dielectric fluid containing 25% PCBs that had leaked from the transformers. NYSDEC then request that EPA perform a removal action because there were signs that trespassers had accessed the property through a broken chain link fence. In addition to broken windows and burned trucks, the property was used by dirt bikers. The surrounding area was occupied by 9500 residents and a school.

In 1994, EPA requested the defendant to perform the removal action and when negotiations failed, EPA issued a unilateral administrative order (UAO) to remove the PCBs from the site. Timmons performed some of the actions required under the UAO, but failed to fully comply with the UAO. EPA then completed the removal action in 1999 at a cost of $1.3 million. In 2000, EPA issued a section 104 Information Request to Timmons and a PRP notice in 2001. When Timmons failed to adequately respond to the information request, the federal government filed a cost recovery action and sought civil penalties for failing to comply with the information request.

Timmons asserted it was not liable under CERCLA because the PCBs had been released prior to its ownership and it had never used the transformers though they remained available for use by proposed commercial tenants. Timmons also asserted that it was entitled to the innocent purchaser and third party defenses.

The court ruled that Timmons did not qualify as an innocent purchaser because the Phase I had identified the PCB-contamination and therefore knew about the release of hazardous substances. The court ruled that Timmons could not assert the third party defense because the security breaches and trespassing was evidence that Timmons had failed to take adequate precautions against the foreseeable acts of third parties. Finally, the court found that Timmons had not exercised due care by failing to remediate the PCB-contamination identified in the pre-acquisition Phase I report and not complying with both the UAO and the information request.

Commentary: *This case demonstrates the limited protection offered by "free and clear" sale orders when the acquired asset is real property. Even if the order relieves the buyer from responsibility for pre-existing releases, the purchaser as a current owner of contaminated property would still have continuing obligations under the Small Business Liability Relief and Brownfields Revitalization Act, signed in 2002, and the Innocent Purchaser, Bona Fide Prospective Purchaser and Contiguous Property Owner defenses (CERCLA Landowner Liability Protections), such as exercising due care or reasonable steps as well as complying with land use controls, cooperating with responsible parties implementing cleanups, providing access to the site and complying with all reporting requirements or information requests.*

The lessons learned from this case are not limited to bankruptcy sales, but applicable to any acquisition of contaminated property. It is not enough for a purchaser to perform a Phase I environmental site assessment that satisfies the requirements of the All Appropriate Inquiry (AAI) rule or the ASTM E1527-05 standards. As EPA repeatedly stated in the preamble to the AAI rule, conducting an AAI/ASTM compliant Phase I is only the first step in ***establishing*** *the CERCLA Landowner Protections. To* ***maintain*** *these liability protections, purchaser must comply with a host of post-acquisition continuing obligations. In this era of risk-based cleanups, it is important that purchasers understand the environmental conditions at the property and ensure that they satisfy all conditions imposed by NFA letters and land use controls that may have been imposed upon the property. It is important that Phase I reports do not simply state that an NFA letter was issued, but also that a copy of the NFA or closure letter be reviewed to determine if there are any post-remedial obligations that may not be recorded in the land records. It is also advisable that consultants evaluate the scope of the investigation and remedial objectives to assess the likelihood that an agency might exercise a reopener due to new cleanup standards or regulatory initiatives such as vapor intrusion. If the Phase I identifies possible reopeners or post-remedial obligations, the purchaser could then negotiate the financial impacts of the issue prior to the closing.*

California Redevelopment Agency Barred From Seeking Injunction Compelling Cleanup

A federal district court ruled that a local redevelopment agency that owned contaminated land for 16 years could not show irreparable harm and therefore was not able to compel a responsible party to remediate the contamination prior to the start of redevelopment project.

In *Redevelopment Agency of the City of Stockton v. Burlington Northern and Sante Fe Railway Corporation*, 2006 U.S.Dist. LEXIS 18319 (E.D.Cal. 4/11/06), the Agency acquired title to three contiguous city blocks in 1990. During grading activities in July 2004, the agency's contractor

discovered petroleum contamination below a French drain on a parcel known as Area 3 that ran parallel to a railroad spur. After sampling confirmed soil and groundwater contamination, the agency halted construction activities and notified the Central Valley Regional Water Quality Control Board (Board) and the Department of Toxic Substances Control (DSTC). In August 2004, the agency exercised its authority under the Polanco Act and issued a corrective action order to the defendants, demanding that they prepare a remedial action plan. When the defendants failed to respond to the order, the agency implemented the work plan at its own expense and later sold Area 3 to a developer who constructed an office building. When plans for another office building at a second parcel known as Area 24 fell through, the agency issued another corrective action order and sought preliminary injunction under the Polanco Act when the defendants failed to respond.

The agency asserted that it would suffer irreparable harm because potential developers were deterred from building on the contaminated parcels and, consequently, it was losing tax revenue. In addition, the agency said it remediated the contamination and filed a cost recovery action because it lacked sufficient resources to remediate all of the contamination in the redevelopment areas. The agency also claimed that money damages were not an adequate remedy for environmental injury.

To obtain a preliminary injunction, the moving party must show a strong likelihood of success, irreparable injury, the balance of hardships must favor the party seeking the injunction and the injunction must be in favor of the public interest. The federal district court said the contamination had occurred at least twenty years ago and the agency had failed to show why waiting a few more months until the conclusion of a trial would pose a significant and immediate threat to the environment. Moreover, while a developer had walked away from a project on one of the parcels because of the contamination, the court said that the agency had not shown that the proposed project was unique or fleeting. In addition, the court found that an award of money damages would be sufficient to compensate for any lost tax revenue. As a result, the court concluded that the agency had not demonstrated how it would be irreparably injured if the remediation was not completed within three months.

The court also held that the agency failed to allege facts of law that clearly showed it would likely prevail on the merits. The court noted that Ninth Circuit precedent provided that prior owners are not responsible for passive disposal and that the state Water Code requires a showing that the prior owner caused the contamination or had actual knowledge of the discharge. Because the facts surrounding the defendants' ownership were ambiguous, the court said it was impossible to determine whether any of the defendants owned or operated the property at the time of the disposal. The court also noted that the record did not indicate who was

responsible for the French drain, when the leak occurred, if the contamination was a result of a slow or sudden leak, or if the defendants had any knowledge of the French drain or contamination. While the agency had raised serious questions, the court held the agency had not demonstrated a likelihood of success on the merits that would be sufficient to warrant a mandatory injunction.

The court acknowledged that a cleanup of the two parcels would impose a hardship on the agency because of the development delays and lost tax revenues. However, because the agency had owned the land for 16 years, the court found that the hardship imposed on the agency did not compare to the burden that would be imposed on the defendants to prepare and implement a costly cleanup on property they no longer own and operate and for which they may not be considered a responsible party.

Finally, while recognizing that eliminating blight conditions would provide public benefits, there were equally important public interests in not prematurely imposing liability on parties who may not be legally responsible for contamination. Since these were equally important public interests at stake, the agency could not demonstrate that the public interest was clearly in its favor.

Commentary: *In prior issues, we have discussed how eminent domain can be a powerful tool for facilitating brownfield development if used effectively. In other jurisdictions with more expansive views of liability under federal or state environmental or common laws, a local agency might have prevailed. Prior to taking title, redevelopment agencies should perform comprehensive environmental due diligence to identify contamination and evaluate the liability of potentially responsible parties*.

Landlord May Recover Costs for Closure of Wells For Monitoring Pre-existing Contamination

In December 1994, Calgon Incorporated (Calgon) entered into a ten-year lease for an office/ warehouse/manufacturing facility. In 2000, Calgon and Nalco Company (Nalco) merged and Nalco assumed the lease. For reasons that are unclear, Nalco installed five groundwater monitoring wells that detected dicholorethene (DCE) above state groundwater standards. The South Carolina Department of Health and Environmental Control (DHEC) subsequently allowed Nalco to abandon three wells but required the two remaining wells to be monitored on a quarterly basis. After the lease expired, Nalco advised DHEC it would not be responsible for financing future monitoring obligations. The landlord was forced to assume responsibility for the wells and after receiving permission to abandon the wells, filed a breach of lease claim.

In *EZE Management Properties Limited Partnership v. Nalco Company*, 2006 U.S. Dist. LEXIS 19897 (D.S.C. 3/30/06), the court ruled that the lease only required Nalco to indemnity the plaintiff for environmental contamination caused by the tenant and there was no evidence that the

tenant had used or stored any hazardous substances that would have caused the contamination. However, because Nalco had not obtained permission from EZE to install the wells and at least one prospective tenant had refused to lease the premises because of the existence of the groundwater monitoring wells, the court determined that Nalco had breached the lease and EZE was entitled to the costs for monitoring or abandoning the wells.

The court denied the motions for summary judgment for both parties that the presence of the wells entitled the landlord to holdover rent and for damages for its inability to re-lease the property rent.

Commentary: *CERCLA and most state environmental laws allow parties to contractually allocate environmental liability. While the contractual allocations are not binding on government agencies, they are enforceable between the parties. Prior to acquiring a business operating under a lease or extending financing to a tenant, it is important to review leases during environmental due diligence to determine if the parties have negotiated responsibility for environmental matters that differs from the statutory framework.*

Property Owner May Bring Citizen Suit For 20-Year old RCRA Violation

Section 7002 authorizes citizen suits for ongoing violations of RCRA and for injunctive relief for past or current storage, use, treatment or disposal of hazardous wastes that are contributing to an imminent and substantial endangerment. In *Hodgins v, Carisle Engineered Products, Inc.*, 2006 U.S. Dist. LEXIS 11321 (E.D.Oh. 3/20/06), a federal district court was faced with the question of whether a generator that stored hazardous wastes at its facility for six years and never registered as a RCRA TSD, but then removed the wastes in 1987, could be liable for civil penalties and injunction to remediate groundwater contamination.

In this case, the Ohio EPA (OEPA) inspected the defendant's facility in 1994 and ordered it to implement "generator closure" for the portions of the property where the hazardous and non-hazardous wastes had been previously stored. The defendant found two separate areas of groundwater contamination on its property as well as a plume that affected the plaintiff's property. However, the OEPA determined that the defendant's facility was not a source of the contamination at the plaintiff's property and the Department of Health determined that the defendant's property did not pose a public health hazard.

The plaintiff then filed its RCRA citizens suit. A magistrate issued a report finding that the failure to comply with the TSD regulations for the storage of hazardous wastes for six years (such as retaining records and filing reports) constituted a continuing obligation. The defendant objected, claiming that since it had not stored wastes at the facility since 1987, the violations were "wholly past" for which no relief was available. However, the court ruled that the TSD regulations

included obligations to maintain records and file reports, which did not expire when waste was no longer stored at the facility. Since the failure to comply with these continuing obligations constituted a present violation, the court ruled that the plaintiff was entitled to judgment as a matter of law. The magistrate recommended that no injunctive relief be granted because wastes had not been stored at the property for 15 years.

The plaintiff objected to this finding of the magistrate, arguing that injunctive relief was appropriate once there was a violation of a statute designed to protect the environment. However, the court said the grant of an injunction was to ensure compliance with a statute and that a court was mechanically obligated to grant an injunction for every violation of law. Noting that RCRA was enacted to reduce generation of hazardous wastes and that no wastes had been stored since 1987, the court found the harm posed by the violation was minimal at best and the purposes of RCRA would not be advanced by injunctive relief.

Finally, the plaintiff sought imposition of civil penalties for the RCRA violations. The court ruled that the amount of any penalties would be determined after a trial on the merits.

Commentary: *As we have discussed in prior issues, RCRA is becoming an increasingly popular tool for property owners to compel cleanups of their properties. However, the plaintiffs must show that the past or present handling of hazardous wastes were contributed to a condition posing a imminent and substantial endangerment to the environment. Courts differ on what constitutes an substantial endangerment with some courts finding any amount of contamination sufficient, while others require contamination above state cleanup levels or that groundwater is actually being used.*

DUE DILIGENCE/ DISCLOSURE

Return of "At-Risk" Cleanup

During the 1980s, it was not uncommon for owners or operators of sites contaminated with petroleum from leaking underground storage tanks (USTs) or releases of other hazardous substances to perform site cleanups without any regulatory oversight in what came to be called "at-risk" or "self-directed" cleanups. Many states established formal remedial procedures that required approval by the state environmental agency, but did not require issuance of a formal completion document or no further action (NFA) letter. Instead, the state environmental agency often would simply accept the final report submitted by an environmental consultant or perhaps orally advise the consultant that the remedial work was satisfactorily completed.

The lack of a decision document providing a formal release from liability was frequently identified as one of the obstacles to redeveloping underused or abandoned contaminated properties. As a result, most of the state brownfield reforms of the 1990s provided that a formal decision document with a covenant not to sue would be issued upon completion of the approved remedial actions.

Recently, though, we have begun to see strong anecdotal evidence that property owners and developers are declining to seek state involvement when contamination is discovered but, instead, electing to remediate the contamination "at-risk." A confluence of factors seem to be at the heart of the growing popularity of self-directed cleanups. Perhaps the most important reason is the spiraling cost of construction and rising interest rates. Construction managers are under enormous pressure to complete projects within budget and often times have financial incentives to complete projects ahead of schedule. As a result, project managers are loathe to report contamination and subject their construction schedules and budgets to the inexorable delays that are associated with understaffed regulatory agencies.

Another important factor is the increasing availability of risk-based cleanups. In states that allow risk-based cleanups, developers are willing to adhere to their construction schedule and gamble that in the event overworked regulators learn about the undisclosed contamination, they will not squander limited enforcement resources on a redeveloped site that does not have any exposure pathways because groundwater is not used for drinking water and contaminated soil is covered by a building foundation or parking lot.

In some states that may be viewed as "pro-development," project managers may also feel that regulators will be reluctant to bring enforcement actions against companies that are converting sites to productive use, generating significant taxes to the local economy.

Commentary: *Developers who are inclined to use "at-risk" or "self-directed" cleanups should consult with local environmental counsel to determine if they have an obligation to report the discovery of historical contamination at a site and not rely on opinions of their environmental consultants. In addition, developers and property owners should use reputable environmental consultants to determine the scope of the investigation and the appropriate level of cleanup that should be implemented at a site, particularly in states without licensed environmental professional (LEP) programs. Otherwise, the developers or property owners may find the cleanup decisions questioned by their lenders.*

Likewise, lenders who are considering using as collateral properties that have undergone an at-risk cleanup should carefully review the documentation generated in connection with the cleanup. In particular, lenders should assess if the investigation was sufficiently comprehensive to have identified all of the contamination at the site, examine the assumptions used in developing the remedy, and evaluate if the remedy was performed in accordance with state requirements.

Lenders should be particularly cautious about self-directed cleanups in states without formal LEP programs. National or regional environmental consulting firms are less likely to succumb to pressures from a client to minimize environmental investigatory and remedial costs because of their large client base and well-established QA/QC protocols. Likewise, LEPs will not want to risk their professional licenses or reputation by failing to comply with state reporting requirements or knowingly violating state protocols. Thus, lenders should consider only lending on sites with self-directed cleanups performed by consultants on the lender's approved list or have one if those approved vendors review the cleanup.

The question the lender should ask itself is, "Would it foreclose on the property if the borrower defaulted?" If after reviewing the cleanup documentation, the lender has any doubts about the adequacy of the cleanup or whether state requirements even allow self-directed cleanups, the lender should require the borrower to disclose the existence of the contamination and the documentation supporting the cleanup to the state regulator and require the borrower to obtain a NFA letter of its equivalent.

Ringwood Mines/Landfill Site Placed Back on NPL

Last fall, we reported on the discovery of paint sludge and other hazardous wastes at residential properties and a state park located near the Ringwood Mines/Landfill Superfund site that had been removed from the National Priorities List (NPL) in 1994. For the first time in the history of the federal Superfund program, EPA announced in April that the Ringwood site would be relisted on the NPL.

The Ringwood Mines/Landfill site contains abandoned mine shafts and surface pits from magnetite mining operations that were conducted from the mid 1700s through the early 1900s. In 1965, the

Ringwood Realty Corporation (Ringwood), a wholly owned subsidiary of the Ford Motor Company (Ford), bought the property and disposed of industrial wastes in the form of car parts, paint sludge and waste solvents generated by Ford's nearby Mahwah assembly plant in the natural depressions, open mine pits and mine shafts located on 150 acres of the 500-acre parcel. Ringwood subsequently sold portions of the property to a developer and donated additional acreage to the local solid waste management authority that operated a municipal landfill from 1972 to 1976. Part of the site also became part of a state park. After remedial measures were implemented between 1987 and 1991, the Agency for Toxic Substances and Disease Registry (ATSDR) concluded that there were no completed human exposure pathways and EPA removed the site from the NPL in 1994. Following discovery of additional paint sludge in the late 1990s, EPA ordered Ford to implement a five-year Environmental Monitoring Program (EMP) consisting of additional response actions and collecting further groundwater and surface water sampling. In 2002, EPA and NJDEP determined that Ford had completed the EMP. The agencies subsequently required Ford to undertake additional remedial actions after discovery of hardened paint sludges on several residential properties.

In a related action, the ATSDR announced that it had completed a health assessment of the Ringwood site and determined that the site posed a "health hazard," which is the second highest risk category in the ATSDR ranking system. The ATSDR assessment concluded that residents were exposed to elevated levels of heavy metals principally lead, antimony, chromium and arsenic from direct contact with paint sludge and contaminated soils and surface waters. They also face an indeterminate risk from volatilization of contaminants as well as from ingestion of wildlife and drinking water from off-site wells. The report found a higher proportion of children with elevated blood lead levels and a slightly higher average childhood blood lead level in the focus area closest to the Ringwood Mines/Landfill site compared to the rest of Ringwood Borough. While ATSDR found that the overall cancer incidence was not elevated, lung cancer incidence was statistically elevated in males in the area closest to the Ringwood Mines/Landfill site. Other possible health concerns that were identified include respiratory diseases, reproductive and developmental effects, neurological disorders, heart disease, skin rashes and eye irritation, anemia, and diabetes. As a result, ATSDR recommended remediation of remaining soil and groundwater contamination and implementation of an Exposure Investigation that would include sampling of indoor dust, soils around residences as well as medical monitoring of as many as 900 adults and children.

Commentary: *The Ringwood site is just one of several sites where concerns have been recently raised*

about the adequacy of past response actions conducted by EPA. For example, the Massachusetts Department of Public Health (DPH) released a study concluding that residents living near the 35-acre former Nyanza Chemical Waste Dump Superfund Site had cancer rates of up to 13 times the rate that would normally be expected. As a result of the study, EPA will be conducting indoor air samples from homes located above contaminated groundwater. An earlier study, completed by EPA in 1999 using less stringent volatility criteria, had concluded that there were no health risks associated with the volatilization of chemicals from contaminated groundwater.

These examples illustrate the importance of requesting and carefully reviewing documentation relating to prior cleanups. Potential owners and their lenders should evaluate the adequacy of remedial investigations that were performed, verify that the appropriate cleanup standards were used, that environmental conditions or standards have not changed that could trigger reopeners, and that any land use controls have been properly implemented.

PCB-Contaminated Fill Material Disposed at Seven New Jersey Redevelopment Sites

Due to the scarcity and cost of aggregate or fill material, contractors often use pulverized construction debris from other construction sites as fill material. Despite the fact that construction and demolition (C&D) debris can contain asbestos, lead-based paint, oil and PCBs, most states do not strictly regulate C&D waste streams. Those states have established management practices for C&D have usually adopted qualitative protocols (descriptions of the waste stream) instead of quantitative protocols (sampling) to determine how to manage various types of C&D debris.

The improper disposal of contaminated fill material generated during the demolition of the former Ford automotive plant in Edison, NJ illustrates the risk associated with lax attention to the type of fill material imported to construction sites. The NJDEP allows concrete to be recycled so long as it is sampled for a variety of contaminants, including PCBs. Concrete debris with 0.49 parts per million (ppm) or less of PCBs can be used as clean fill at residential projects while concrete with up to 2 ppm may be used at non-residential sites and as road bed. Concrete debris with more than 2 ppm of PCBs must be disposed at a PCB-licensed landfill.

After Ford closed the Edison plant in February 2004, Ford estimated the plant cleanup costs would be at least $46 million. To minimize its demolition costs, Ford offered to provide concrete debris for free to any contractor or developer who was willing to haul away the material. Ford's demolition contractor sampled the debris and segregated it into three separate piles. One pile was for debris that sampling had shown was "non-detect" for PCBs, a second pile contained debris that had between 0.49 and 2 ppm of PCBs and the third pile was for debris that had more than 2 ppm

PCBs and had to be disposed at a landfill. Ford sold the concrete debris at no cost to several developers including Edgewood Properties who brought in its own contractor to pulverize the concrete for use as aggregate at several development sites. It appears that Edgewood's contractor may have mixed pulverized concrete from all three piles because 11 sites that received the aggregate from the Edison plant have been found to have PCB-contaminated fill material. Several of the sites are residential projects. NJDEP subsequently ordered Ford to collect samples from 40 residential properties near the Edison plant and to remove the PCB-contaminated fill from all locations that received the tainted fill material. The South Plainfield planning board recently rejected a proposal to build a nearly 500-unit age-restricted housing complex on the site of the former Tingley Rubber Plant because of the PCB contamination.

Commentary: *The Edison plant fiasco is just the latest in a series of incidents involving contaminated fill material. For example, last fall, we reported on the residential project in Kalmath Falls, OR, where asbestos-containing debris was found and residents were relocated by EPA. In Providence, RI, EPA is excavating contaminated fill material from 30 residential properties. Prior to its development, the area had a natural depression that developers filled with auto fluff to bring the site up to grade. In another case of contaminated fill, the Massachusetts DEP ordered all work to cease at a construction site in Leominster after pulverized pieces of transite piping was discovered.*

Luxury developments are not immune from the dangers of contaminated fill material either. The Bay Harbor resort overlooking Lake Michigan has a highly rated golf course, yachting and equestrian clubs, stylish boutiques and million-dollar mansions with breathtaking views of the lake. It was also built on the site of the former Penn-Dixie Cement Company facility where 2,500 barrels of limestone per day were quarried, crushed, baked in kilns and four enormous heaps of kiln dust left behind when the plant was shut down in 1981. Contaminated discharges were identified during the redevelopment, but the Michigan DEQ (MDEQ) concluded that the discharge was not associated with the kiln materials because it was believed not to be leachable. Local environmental groups requested that a landfill-quality liner and cap be installed in the area of the dust piles, but the developer resisted that suggestion because of the costs. Instead, MDEQ approved a pollution prevention plan that called for constructing a golf course and park atop the waste piles, which would be covered with soil and greenery. After discharges with alkaline levels similar to industrial bleach and heavy metals was found seeping from the buried cement dust piles into Little Traverse Bay, the MDEQ restricted access to about 7,000 feet of the 5-mile shoreline and shutdown an adjacent public park created by the resort. According to some residents, property values have plummeted and they have been unable to sell their property. Meanwhile CMS Energy

Group estimates that the cleanup of the resort will cost $85 million.

There have been instances where developers have spent millions of dollars to remediate sites only to have them re-contaminated with fill material. State environmental agencies simply do not have the resources to track the volume of C&D generated by construction sites and contractors looking to increase profit margins have little financial incentive or time to find clean fill. Thus, it is important that developers establish a system to screen the fill materials that are to be imported to their development sites.

Most State Dry Cleaner Trust Fund Rankings Ignore Vapor Intrusion

Many consultants conducting due diligence on PCE-contaminated sites that have been assigned a low priority ranking in state dry cleaner programs often rely on that low priority to conclude that the release does not pose a significant risk to the Property. However, an informal survey conducted by SEJ has found that very few states take the vapor intrusion (VI) pathway into account when ranking a site for purposes of a fund-financed cleanup. It appears that site rankings in states that conduct fund-financed cleanups were principally based on threats to drinking water supplies. If the PCE has not impacted groundwater or has contaminated groundwater that is not being used for drinking water purposes, then the site will tend to receive a low priority ranking.

According to our survey, those states that do evaluate vapor intrusion tended to be states with programs that reimburse property owners for cleanups rather than fund the cleanup at the outset. In these states, property owners may receive reimbursement only if they implement an approved remedial action work plan (RAWP) and the state agency will not approve the RAWP unless the vapor intrusion pathway has been valuated.

Commentary: *As we discussed in our prior issue, there is considerable disagreement in the legal and consulting community as to whether VI is a REC under ASTM E1527, an impact of a REC or a non-scope consideration. Too often, environmental professionals are getting caught up in a technical analysis as to why VI should not be a REC without looking at the bigger picture. The fact is that most Phase I reports are being performed to assess business risks and not to simply assert the CERCLA landowner defenses, which are largely illusory. The owner of a shopping center located near residential properties that will not be remediated by a state fund for five to ten years because of a low ranking based on absence of groundwater receptors might not be liable for a cleanup; however, they could still face the business risk of toxic tort and property damage/stigma claims if the release of PCE migrates to adjoining properties during the five to ten year period and creates a vapor intrusion problem.*

For example, EPA is currently investigating whether PCE from the former VIP Cleaners facility in Morristown, NJ is posing a risk of vapor intrusion in nine residential buildings and 21 commercial

buildings in the area. EPA has collected samples under several businesses that now operate in the former dry cleaner's building, inside nearby businesses, and under basements of nearby homes. In November 2005, EPA confirmed that PCE and TCE were in the groundwater beneath the buildings but were not impacting drinking water.

Until the ASTM Vapor Intrusion Task Force issues its standard, consultants should consider vapor intrusion from a risk management standpoint to minimize the possibility that they could become subject to negligence actions or breach of contract actions for failing to flag a potential vapor intrusion problem at a site. There are a range of options that consultants could adopt to minimize their exposure such as identifying VI as REC, recommending that the VI pathway be further evaluated for sites impacted with VOCs and petroleum, or making it abundantly clear in their reports and contracts that VI is considered a non-scope consideration that will not be evaluated unless specifically requested by the client.

More Claims Filed Against Consultants for Phase I Reports

Insufficient historical investigations and a misunderstanding of local cleanup standards were the basis for claims that were recently filed against consultants preparing Phase I reports.

The deficient historical investigations occurred on two California hotels. In the first case, the Phase I ESA failed to report that a gas station had operated on a portion of the property for over thirty years. Despite the fact that the presence of a gas station was obvious on three Sanborn maps from the 1950s, the consultant did not discuss the prior gas station or make any recommendations. Since the former gas station was located on the portion of the property that was now occupied by a parking lot, it was still possible that the tanks and impacted soils might still be present on the property. The owner of the property is now conducting an investigation and is seeking the costs of any investigation and remedial costs from the consultant.

In the second California case, a Phase I failed to the discover that the property was built on a former landfill. When the owner decided to refinance, a subsequent phase I ordered by a bank identified the former landfill. As a result, the lender is requiring further investigation to verify that the former landfill does not pose a risk to the Property.

Our last example involves a Phase I performed for a purchaser of a site in Florida. The consultant indicated that arsenic detected in soil and groundwater was below state cleanup standards and did not require any further action. The client then proceeded to purchase the property. As it turns out, the Phase I report failed to note that the state had recently tightened its groundwater standards and that the arsenic concentrations exceeded the groundwater cleanup standards. After the client filed a negligence action against the consultant, the parties reached a settlement.

SEC Staff Recommends Enforcement Action for Change To Environmental Reserves

There has been considerable speculation on what effect Sarbanes-Oxley and Financial Accounting Standards Board Interpretation No. 47 (FIN 47) will have on environmental disclosure. Despite these tighter reporting standards, the popular belief is that companies may not start taking a hard look at their environmental disclosure policies until the Securities and Exchange Commission (SEC) commences a high-profile environmental action. A recent announcement by the SEC staff may put that view to the test.

On April 25, 2006, Ashland, Inc.(Ashland) was notified by the SEC staff that the staff will seek authorization to seek injunctive and/or administrative relief for adjustments that reduced environmental remediation reserves for fiscal years 1999 and 2000. These adjustments to environmental reserves totaled $12.2 million in 1999 and $12.6 million in 2000. However, the SEC staff did not recommend assessment of any fines, penalties or restatements from Ashland nor allege any intentional misconduct by Ashland.

Commentary: *Since FIN 47 became effective in December 2005, many law firms have issued client alerts explaining how FIN 47 may accelerate the accrual of environmental liabilities on corporate balance sheets and increase the amounts of their environmental reserves. According to one analyst, there have been 43 examples where companies have recorded asset retirement obligations that had not been identified prior to the implementation date of FIN 47.*

A minority of law firms have taken the position that because FIN 47 only applies to conditional asset retirement obligations (CAROs) associated with "normal operation" of the asset, most environmental remediation obligations should not be CAROs and therefore would not have to be reported under FIN 47. The rationale of this minority view is that environmental contamination is a result of spills or unplanned releases that are not a result of the proper or "normal operation" of an asset. Under this interpretation, recognition of environmental cleanup obligations would continue to be governed by SFAS 5 and SOP 96-1.

We believe that this minority position is incorrect because it ignores the fact that EPA has established design standards for various types of hazardous waste management units and USTs precisely for the reason that leaks, spills and discharges of hazardous wastes were a part of the operation of those facilities.

While companies grapple with FIN 47, the Financial Accounting Standards Board is considering lowering the threshold for recognizing losses from pending litigation. Under Financial Accounting Standard 5, Recognition and Measurement in Financial Statements of Business Enterprises, public companies must disclose lawsuits when it is probable that they will result in a loss. This requirement has generally meant that there is an 80% probability that the company

would lose. FASB is considering lowering the trigger so that companies would have to report the potential damages from a lawsuit when it "more likely than not" or "reasonably possible" that the company would not prevail. Under this approach, a company would have to report losses from lawsuits when there was a 51% probability that the company would lose the case. There is even some speculation that FASB may adopt the "fair value" approach used in FIN 47 and the International Accounting Oversight Board.

Vapor Intrusion Bill Introduced In California Legislature

Two bills working their way through the California legislature would create new requirements for sites with potential for vapor intrusion.

Under AB 2092, the California Environmental Protection Agency (Cal EPA) would work with the Department of Toxic Substances Control (DTSC), the State Water Resources Control Board (SWRCB), the regional water boards, the Integrated Waste Management Board (CIWMB), and the appropriate local agencies including the redevelopment agencies, to create a comprehensive list of the sites in California with known or potential vapor intrusion from a hazardous substance release on or near the site by January 1, 2008. CalEPA would also be required to post a summary of on its website identifying sites that could pose significant health and safety risks based on modeling as well as sites with known or potential vapor intrusion, as determined by regulations developed by the agency with jurisdiction over vapor intrusion. If any of the agencies does not have regulations governing vapor intrusion, the agencies shall use regulations adopted by the DTSC or the screening protocols issued by the San Francisco Regional Water Quality Control Board. The Brownsfield ombudsman would be required to work with appropriate state or local agencies and property owners to develop a strategy and implementation schedule for identifying other sites with potential vapor intrusion. The Brownfield ombudsman would also submit a report for developing a uniform strategy for remediation, engineering and land use controls, and legal mechanisms to assure long-term maintenance of controls for as long as the vapor intrusion presents a human health risk. The legislation originally provided that CalEPA would be required to issue orders to responsible parties for any site with known or potential vapor intrusion from on-site release or contamination migrating onto the site where there is insufficient data to conduct an investigation to determine the extent of a vapor intrusion problem and submit the data to DTSC. However, this provision was deleted in recent amendments.

AB 815 requires the Cal-OSHA Standards Board (Board) to adopt occupational safety and health standards for any hazardous substances for which there is a quantitative risk assessment prepared or published by the Office of Environmental Health Hazard

Assessment (OEHHA). AB 815 also requires the Hazard Evaluation System and Information Service (HESIS) to recommend revised or new standards to the Board if it finds an existing permissible exposure limit (PEL) is not as protective as HESIS's, or if no PEL is in place for a workplace hazardous substance that is listed as known to the state to cause cancer or reproductive toxicity. Currently, HESIS is required to recommend occupational safety and health standards whenever it determines that a substance in use at California workplaces is potentially toxic to workers. AB 815 would require the Board to adopt occupational safety and health standards for any continued hazardous substances for which OEHHA has prepared or published a quantitative risk assessment. HESIS would be required to revise existing PELS by January 1, 2008, and by January 1, 2009, HESIS would issue standards for substances without PELs and which are listed under Proposition 65 as cancer causing or causing reproductive toxicity. AB 815 also requires HESIS to recommend revised or new standards to the Board if it finds an existing PEL is not as protective as HESIS's, or if no PEL is in place for a workplace hazardous substance that is listed as known to the state to cause cancer or reproductive toxicity. Finally, AB 815 requires HESIS to develop risk levels that it will use to derive air concentration levels for hazardous substances prior to or in conjunction with the development of any PEL HESIS recommends to the Board.

Finally, a bill has been introduced to clarify what agencies have jurisdiction for vapor intrusion at workplaces. Under the proposed legislation, Cal-EPA would have jurisdiction for exposures to VOCs resulting from chemicals used in the workplace. However, when the exposure is due to vapor intrusion emanating from releases to soil or groundwater contamination, the bill would confer jurisdiction to Cal-EPA

Rhode Island Attorney General Seeks to Hold Up Sale of Utility

The state utility authority will allow the state attorney general to intervene in an action that seeks to block a $498 million sale of New England Gas' Rhode Island assets to National Grid.

A group of 129 residents in Tiverton filed a lawsuit in federal district court seeking to block the sale because they are concerned that the parent of New England Gas, Southern Union, could pay for a cleanup if the proposed deal is approved. The Department of Environmental Management (RIDEM) has determined New England Gas responsible for the cleanup as a successor to the company that allegedly disposed of arsenic and other hazardous wastes on land that is now occupied by 100 residences.

While the board allowed the attorney general to intervene in the action, it also ruled that the Tiverton residents do not have standing to intervene in the case because they represent a private interest, not a public one. New England Gas is a division of Houston-based Southern Union, a publicly traded company with assets worth $5.8 billion.

Commentary: *Environmental authorities and community groups are frequently seeking to intervene in utility sales and bankruptcy proceedings to ensure that adequate funds are set aside to address contamination associated with the assets to be sold. This trend has accelerated in the wake of the Asarco bankruptcy (discussed in the litigation section below) where the federal government filed a temporary injunction requesting the bankruptcy court not to approve the plan for reorganization until the adequate financial assurances were established to cover the company's remediation obligations at a number of sites. As a result, it is increasingly important to identify potential remediation obligations in these transactions and anticipate objections to the transactions so that a plan can be proposed that will allow a regulator or bankruptcy court to approve the transaction.*