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The Impact of Environmental Liabilities on Real Estate Contract Negotiations

Gail V. Karlsson*

The author examines environmental issues facing a prospective seller of industrial real property. Because a seller generally will not be able to transfer statutory responsibility for environmental problems, it is advisable for the seller to investigate and remedy environmental problems prior to transferring the property. An environmental investigation may be required for the seller to make representations and warranties to buyers and lenders. Both lenders and buyers will want to conduct some degree of investigation to protect themselves from environmental liability, particularly liability arising from Superfund and similar state statutes. Information gained from environmental investigations can be useful during negotiations for sale and for contractual allocation of environmental responsibility. Where a site cleanup is required, information gained from an environmental investigation can serve as the basis for a remediation plan. As a result of an environmental investigation and site remediation, the seller will be in a stronger position to negotiate limitations on indemnity provisions requested by the buyer. The author concludes that given the current level of environmental awareness and regulation, cleaning up contaminated industrial property is not only good policy, it is good business.

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I. Introduction

The federal Superfund legislation,¹ originally enacted to address the problem of abandoned hazardous waste sites requiring the expenditure of public funds for cleanup operations, has had a tremendous impact on business transactions involving the transfer of industrial plants and real property. Under Superfund, the current owner or operator² of a facility³ contaminated with hazardous substances⁴ can be held strictly liable⁵ for site cleanup costs. The current owner is jointly and

1. The Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA), 42 U.S.C. §§ 9601-9675 (1983 & Supp. 1990), *as amended by* The Superfund Amendments and Reauthorization Act of 1986 (SARA), Pub. L. No. 99-499, 100 Stat. 1613 (1986).

2. "The term 'owner or operator' means . . . any person" 42 U.S.C. § 9601(20)(A). "The term 'person' means an individual, firm, corporation, association, partnership, consortium, joint venture, commercial utility, United States government, State, municipality, commission, political subdivision of a State, or any interstate body." 42 U.S.C. § 9601(21).

3. The term "facility" is defined in CERCLA as:

(A) any building, structure, installation, equipment, pipe or pipeline (including any pipe into a sewer or publicly owned treatment works), well, pit, pond, lagoon, impoundment, ditch, landfill, storage container, motor vehicle, rolling stock, or aircraft, or (B) any site or area where a hazardous substance has been deposited, stored, disposed of, or placed, or otherwise come to be located; but does not include any consumer product in consumer use or any vessel.

42 U.S.C. § 9601(9).

4. In CERCLA, "hazardous substances" are defined at § 101(14), 42 U.S.C. § 9601(14), and include substances identified in § 307(a) and § 311(b)(2)(A) of the Clean Water Act (CWA), 33 U.S.C. §§ 1317(a) and 1321(b)(2)(A) (1988); § 3001 of the Resource Conservation and Recovery Act of 1976 (RCRA), 42 U.S.C. § 6921 (1988), and the regulations promulgated pursuant to it at 40 C.F.R. Part 261 (1990), and § 112 of the Clean Air Act (CAA), 42 U.S.C. § 7412 (1988). Also included are imminently hazardous chemicals to which the Environmental Protection Agency (EPA) has taken action pursuant to § 7 of the Toxic Substances Control Act (TSCA), 15 U.S.C. § 2606 (1988), and any other substance, pollutant or contaminant that the EPA has designated under § 102(a) of CERCLA, 42 U.S.C. § 9602(A) as a hazardous substance. 42 U.S.C. § 9601(14). Petroleum products are specifically exempted, as are natural gas and substances related to it. "Hazardous substances" designated as such by the EPA are also defined and listed at 40 C.F.R. § 302.4 (1990).

5. 42 U.S.C. § 9601(32) defines "liability" as the standard of liability under the CWA § 311(c), 33 U.S.C. § 1321(c). The majority of courts have held that § 9601(32) incorporates strict liability from the CWA. *See, e.g.,* United States v. Monsanto Co., 858 F.2d 160 (4th Cir. 1988); Tanglewood East Homeowners v. Charles-Thomas, Inc., 849 F.2d 1568 (5th Cir. 1988). *See generally* D. STEVER, LAW OF CHEMICAL REGULA-

severally liable,⁶ together with other potentially responsible parties, including the owner and operator at the time the contamination occurred.⁷ This means that if other potentially responsible parties are insolvent, the current owner can be required to pay the entire site cleanup cost, even if he did not contribute to the contamination.

Fear of liability under Superfund for the costs of cleaning up contaminated property has made potential purchasers and lenders increasingly wary of assuming any interest in industrial property without undertaking an extensive environmental assessment.⁸ Although relatively few industrial sites are so contaminated as to become candidates for the Superfund cleanup list,⁹ the costs associated with such a cleanup are so overwhelming that no reasonable purchaser would risk incurring what amounts to an open-ended contingent liability.¹⁰

TION AND HAZARDOUS WASTE § 6.07(1)(a) (1990).

6. Most courts have held that CERCLA provides for joint and several liability in appropriate circumstance. *See, e.g.,* *United States v. Chem-Dyne Corp.*, 572 F. Supp. 802 (S.D. Ohio 1983); *United States v. A & E Materials Co., Inc.*, 578 F. Supp. 1249 (S.D. Ill. 1984). CERCLA neither mandates nor bars joint and several liability but leaves imposition of it to the courts' discretion where the harm is single and indivisible and where there is no reasonable basis for apportionment of damages (*i.e.* divisible injury). *O'Neil v. Picillo*, 682 F. Supp. 706 (D.R.I. 1988), *aff'd*, 883 F.2d 176 (1st Cir. 1989), *cert. denied*, 110 S. Ct. 1115 (1990).

7. Potentially responsible parties (PRP's) include the current owner and operator of a facility, any owner or operator of a facility at the time of disposal of any hazardous substances, any person who arranged for disposal, treatment, or transportation of any hazardous substance, and any person who transported any hazardous substance to disposal or treatment facilities selected by that transporter. D. STEVER, *LAW OF CHEMICAL REGULATION AND HAZARDOUS WASTE* § 6.07(1)(a) (1990).

8. *See, e.g.,* Comment, *When a Security Becomes a Liability: Claims Against Lenders in Hazardous Waste Cleanup*, 38 HASTINGS L.J. 1261 (1987); Cornell, *The Toxic Mortgage: CERCLA Seeps Into the Commercial Lending Industry*, 63 ST. JOHN'S L. REV. 839 (1989).

9. There are over 1200 sites on the National Priorities List. 40 C.F.R. § 300 app. B (1989). The National Priorities List is "the list, compiled by EPA pursuant to CERCLA Section 105, of uncontrolled hazardous substance releases in the United States that are priorities for long-term remedial evaluation and response." *Id.* § 300.5. *See* 42 U.S.C. § 9605(a). This is only a small proportion of the industrial sites in this country.

10. Cleanup costs for Superfund sites have recently averaged \$25 million and are expected to increase. EPA, *A MANAGEMENT REVIEW OF THE SUPERFUND PROGRAM* 3 (1989). The costs are largely unpredictable and may include costs of (a) investigations, testing, and monitoring to identify the dangers to public health, welfare, and

The current regulatory climate has fostered the negotiation and implementation of site cleanups between private parties, in the context of routine business transfers, as a supplement to the government's enforcement efforts.¹¹ Although there would be little incentive for private cleanup activities without the threat of enforcement actions under Superfund or similar state statutes, government agencies have very limited resources for site investigations and tend to focus their efforts on situations where there is an immediate threat to public health or natural resources.¹² Many industrial site owners are unaware of soil and groundwater contamination resulting from past disposal practices. For these owners there is no reason to conduct an investigation until they consider transferring the property. At that point they must anticipate the sort of investigations and representations concerning environmental conditions which will be required by potential purchasers.¹³

Some states, most notably New Jersey,¹⁴ have specific property transfer statutes requiring a property owner to conduct a site assessment and to clean up any existing contamination before the property is transferred. New York has yet to enact such legislation,¹⁵ nevertheless, in many instances pri-

the environment due to the release or threatened release of hazardous substances; (b) planning and implementation of response and remedial actions; and (c) enforcement costs incurred by the staffs of the EPA and the Department of Justice. See *United States v. Conservation Chem. Co.*, 619 F. Supp. 162, 186 (W.D. Mo. 1985).

11. For additional discussion of environmental considerations in private real estate transactions, see generally Fitzsimmons & Sherwood, *The Real Estate Lawyer's Primer (and more) to Superfund: The Environmental Hazards of Real Estate Transactions*, 22 REAL PROP., PROB. & TR. J. 765 (1987).

12. Sites are ranked on the National Priority List on the basis of their relative degree of risk to human health and the environment. 42 U.S.C. § 9605(c). See also *EPA Region III, Based in Philadelphia Tackles Enforcement by Targeting Ways of Using Limited Resources to Deter Violations*, 17 Env't Rep. (BNA) 760 (Sept. 19, 1986).

13. See *infra* notes 34-39 and accompanying text.

14. New Jersey Environmental Cleanup and Responsibility Act (ECRA), N.J. STAT. ANN. § 13:1K-6 to -1K-14 (West 1979 & Supp. 1990).

15. New York State Senate Bill No. 207-89 introduced by Committee on Rules May 1, 1989 and referred to the Committee on Environmental Conservation. S. Res. 207, 212th Sess., 1989 N.Y. Laws 1, would require a seller of commercial property to either certify that the property is not contaminated or present a cleanup plan. In

vate parties have imposed similar restrictions on the transferability of industrial property without government intervention. These restrictions may not seem attractive to a property owner who is unable to sell his property without undertaking costly and time-consuming environmental assessments and remedial activities. However, they do provide an interesting example of how legislative developments can affect market forces and promote environmental remediation by private parties without direct governmental involvement.

Because waste disposal did not emerge as a regulatory concern until the 1970's, many older industrial facilities contain some degree of soil or groundwater contamination as a result of past environmentally unsound waste disposal practices and plant operations.¹⁶ In some cases the property may be so contaminated that remedial costs far outweigh the value of the site to a potential purchaser.¹⁷ More often, environmental conditions have emerged as just another important factor in the negotiation of price and contract terms.

This article examines some of the issues facing a prospective seller of industrial real property and offers certain practical suggestions for addressing site investigations, remedial actions, and contract negotiations.

II. Seller's Site Assessment

In general, if site conditions are not fully known, it is preferable for the owner¹⁸ to conduct a site assessment before putting the property on the market.¹⁹ This allows the seller to

addition, a bill to enact the New York Property Owners Protection Act (POPA) was introduced on March 5, 1990 by Assemblyman Maurice Hinchley, A9676, STATE OF NEW YORK LEGISLATIVE DIGEST, 213th Sess. at 624 (1990). See Privitera, *Where's POPA? It is Time to Enact New York's Property Owners Protection Act*, 6 N.Y. ST. B.J. 33 (July 1990).

16. In 1976, Congress enacted the Resource Conservation and Recovery Act (RCRA), 42 U.S.C. §§ 6901-6992 (1988). Prior to RCRA, the disposal of hazardous wastes was largely unregulated.

17. See *supra* note 10.

18. See *supra* note 2.

19. See generally *Id.* Baker & Markoff, *By-Product Liability: Using Common Law Private Action to Clean Up Hazardous Waste Sites*, 10 HARV. ENVTL. L. REV. 99, 101 (1986). Incentives for current owners to conduct their own site assessment in-

determine whether or not the site is contaminated and to estimate the cost of necessary remedial action,²⁰ if any, before entering into negotiations with prospective purchasers.

Undertaking a site assessment requires hiring a professional environmental consultant to work in conjunction with an attorney experienced in environmental matters.²¹ The consultant will generally gather certain information about current and former operations and then, based on that information and a site inspection, conduct tests and take samples in areas of potential contamination. Possible concerns include: asbestos in buildings,²² leaking underground storage tanks,²³ soil contamination in areas where chemicals were improperly stored or disposed²⁴ of, and resulting surface or ground water contamination. Depending on the results of the site inspection and initial soil and groundwater samples, the consultant may recommend additional sampling to determine the nature and extent of any contamination found. The consultant should then prepare a report describing the condition of the site, recommending appropriate remedial action, if necessary, and estimating the cost of any proposed remedial work.

clude the threat of litigation by "the government or private parties who are harmed by releases, or the threat of releases, from the site." Additionally, "even without litigation, beneficial use or resale of the site may be impossible without restoration or containment." *Id.*

20. CERCLA defines the term "remedial action" as "those actions consistent with permanent remedy taken instead of or in addition to removal actions in the event of a release or threatened release of a hazardous substance into the environment" 42 U.S.C. § 9601(24) (1988).

21. The consultant is responsible for detecting the likelihood of site contamination; the attorney is responsible for placing the consultant's findings in the appropriate legal framework. *See, e.g.,* AMERICAN ENVIRONMENTAL GROUP, *SCREENING REAL ESTATE FOR ENVIRONMENTAL HAZARDS: A PRACTICAL GUIDE FOR ATTORNEYS, LENDERS AND DEVELOPERS* (1989).

22. *See, e.g.,* United States v. Geperr Bros., Inc., 638 F. Supp. 996 (E.D. Pa. 1986).

23. Underground storage tanks are subject to a special regulatory program established in the 1984 re-authorization of RCRA, 42 U.S.C. §§ 6901-6992k (1988). *See generally* Italiano, *Liability for Underground Storage Tanks* (1987).

24. "Disposal" means the "discharge, deposit, injection, dumping, spilling, leaking, or placing of any solid waste or hazardous waste into or on any land or water so that such solid waste or hazardous waste or any constituent thereof may enter the environment or be emitted into the air or discharged into any waters, including ground waters." 42 U.S.C. § 6903(3); 40 C.F.R. § 260.10 (1990).

The risk associated with conducting a site assessment is that the owner may discover environmental violations about which he would rather not have known. Once the consultant's report is completed, the owner might discover that he has a statutory obligation to notify government agencies of site conditions.²⁵ He could then find himself embroiled in extensive cleanup negotiations with government representatives, unable to even consider selling the property in its current condition.

As unattractive as that scenario may be, the alternatives to conducting a site assessment present their own risks. For instance, suppose a seller assumes that the site is clean and enters into a contract of sale without conducting any investigation. If the site is later found to be contaminated, he might find himself in the awkward position of being required to conduct cleanup operations on a site he no longer owns.²⁶ This will further complicate remedial activities as well as negotiations with governmental agencies. It may be difficult to determine which contamination problems were actually caused by the seller and which may have resulted from the buyer's operations after the property was transferred. In addition, it may be difficult for the seller to gain access to the site for sampling and cleanup activities without interfering with the buyer's operations, or without indemnifying the buyer against possible property damage resulting from the contamination or the cleanup activities.

Given the current regulatory and judicial view of liability for environmental damage, the seller generally will not be able to effect a truly "as is" sale of the property. For example, in a

25. 42 U.S.C. § 9603(a). "Any person in charge of a vessel . . . [or] facility shall, as soon as he has knowledge of any release (other than a federally permitted release) of a hazardous substance from such vessel or facility in quantities equal to or greater than those determined pursuant to section 9602 of this title, immediately notify the National Response Center . . . of such release."

Id.

26. CERCLA imposes liability on "any person who *at the time of disposal* of any hazardous substance owned or operated any facility at which such hazardous substances were disposed of" 42 U.S.C. § 9607(a)(2) (emphasis added). A prior owner will escape potential liability under CERCLA only if it is not alleged that he disposed of any hazardous substances during the period of his ownership. *Id.*

ruling on cross-motions for summary judgment, the U.S. District Court for the Eastern District of New York held that the "as is" clause in a land purchase contract did not bar a claim for cleanup costs under Superfund asserted by the current owner against the former owner.²⁷ In *Stevens*, the property was contaminated with hazardous substances by MDI Corp., the former lessee.²⁸ The new owner, International Clinical Laboratories sought reimbursement under Superfund for site investigation and cleanup costs.²⁹ The seller asserted that the reimbursement claim was barred because the contract of sale stipulated that the property was transferred "as is."³⁰ The court ruled that according to New York law, an "as is" clause is effective to preclude only those causes of action based on a breach of warranty theory, not on statutory claims.³¹

Because the seller generally will not be able to transfer statutory responsibilities for environmental problems, it is advisable for the seller to investigate and remedy environmental problems prior to transferring the property.

III. Representations Requested By Buyers

In negotiating a contract of sale, the buyer generally will require the seller to give representations and warranties concerning past and present environmental conditions at the site³² and to indemnify the buyer for any breach of those representations and warranties.³³ Sample representations which might be requested by a buyer include the following:³⁴

27. *International Clinical Laboratories, Inc. v. Stevens*, 710 F. Supp. 466 (E.D.N.Y. 1989).

28. *Id.* at 468-69.

29. *Id.* at 468.

30. *Id.* at 469.

31. *Id.* at 470. See also *Southland Corp. v. Ashland Oil, Inc.*, 696 F. Supp. 994 (D.N.J. 1988) (applying New Jersey contract law).

32. See generally *Emhart Indus., Inc. v. Duracell Int'l Inc.*, 665 F. Supp. 549 (M.D. Tenn. 1987); *Fitzsimmons & Sherwood*, *supra* note 11, at 783.

33. See, e.g., *Nunn v. Chemical Waste Management, Inc.*, 22 Env't Rep. Cas. (BNA) 1763 (D. Kan. Mar. 4, 1985).

34. For additional samples of contract representations and warranties, see J. MOSKOWITZ, ENVIRONMENTAL LIABILITY AND REAL PROPERTY TRANSACTIONS: LAW AND PRACTICE 280 (1989); *Fitzsimmons & Sherwood*, *supra* note 11, at 783.

1. The seller has at all times complied with, and is not currently in violation of, any applicable environmental laws, rules, regulations, or orders of any governmental authorities.³⁵

2. The seller has obtained and complied with all environmental permits, registrations, and authorizations required under all environmental laws, rules, and regulations applicable to its business.

3. The seller has not received any notice of violation or penalty assessment with respect to any environmental law, rule, or regulation and no investigation or review is pending or threatened by any governmental authority with respect to any alleged violation of any environmental law, rule, regulation, or order.

4. There are no actions, suits, claims, or proceedings pending or threatened relating to the use, maintenance, operation, or condition of the sale property, nor is there any basis for any such action, suit, claim, or proceeding being instituted or filed.

5. The seller has not generated, treated, stored, recycled, or disposed of on the sale property any hazardous substances (as defined in federal, state or local laws, ordinances or regulations), nor has anyone else treated, stored, recycled, or disposed of hazardous substances on the sale property, except in strict compliance with all environmental, health, or safety laws, rules, and regulations.

6. No hazardous substances have been released, spilled, leaked, discharged, emitted, leaked, or allowed to escape at, on, or under the sale property.

7. No notification of a release or threat of release of a hazardous substance has been filed by the seller or any other party with respect to the sale property, and the sale property

35. Some states have enacted property transfer statutes dealing with hazardous substances which may require specific representations regarding environmental conditions at the site. *See, e.g.*, N.J. STAT. ANN. § 13:1K- 6 to 1K-14 (West 1979 & Supp. 1990); Indiana Responsible Party Transfer Law, IND. CODE ANN. § 13-7-22.5 (Burns 1990); Illinois Responsible Party Transfer Act of 1988, ILL. ANN. STAT. ch. 30 para. 901-907 (Smith-Hurd 1969 & Supp. 1990); Connecticut Transfer of Hazardous Waste Establishments Act, CONN. GEN. STAT. ANN. §§ 22a-134(3)-134(d) (West 1985 & Supp. 1990).

is not listed or proposed for listing on the National Priorities List³⁶ promulgated pursuant to Superfund or on any similar state list of sites requiring investigation or cleanup.³⁷

8. No PCBs, asbestos, or urea formaldehyde insulation are, or have been, present on the sale property.

9. There are no underground storage tanks, active or abandoned, located on the sale property.³⁸

10. There are no environmental liens on the sale property.³⁹

11. The seller has provided the buyer with reports of all environmental inspections, investigations, studies, audits, tests, or other analyses conducted at or in connection with the sale property.

12. The seller is not aware of any facts related to environmental conditions at the sale property which could lead to any future environmental claims or liabilities.

13. There are no environmental laws, rules, regulations, or orders relating to environmental matters requiring any work, repairs, construction, or capital expenditures with respect to the sale property.

The seller will not be able to make many of these representations without having completed a site assessment. He might be able to avoid making certain representations and limit others by stating that they are true "to the best of his knowledge;" but in that case the buyer would likely respond by requiring a broader indemnification against future environmental claims.

The seller can also attempt to limit his exposure with respect to the breach of environmental representations in a

36. See *supra* notes 9 & 12.

37. In New York State, for example, the Department of Environmental Conservation must compile and update annually a registry identifying every inactive hazardous waste disposal site in the state. See N.Y. ENVTL. CONSERV. LAW § 27-1303 (McKinney 1984 & Supp. 1991).

38. See *supra* note 23.

39. CERCLA provides for a lien against real and personal property that is subject to a federal response action. CERCLA § 107(l), 42 U.S.C. § 9607(l). In addition, some states have enacted lien laws to allow states to recover costs of government cleanups of hazardous waste sites. See, e.g., CONN. GEN. STAT. ANN. §§ 22a-452a (West 1958 & Supp. 1990); N.J. STAT. ANN. §§ 58:10-23.11f (West 1982 & Supp. 1990).

number of ways. He could specify in the contract that the representations are made exclusively for the benefit of the buyer and cannot be relied upon by any successor or other third party, he could limit the period of time for which the representations will survive the closing, he could require that the amount of any claim or claims for breach of the representations must exceed a certain amount before the buyer is entitled to compensation, he could limit the total amount that the buyer can claim for breach of the representation, or he could specifically disclaim liability for incidental or consequential damages resulting from a breach of the representations.

IV. Buyer's Site Investigation

From the buyer's perspective, one reason for placing environmental representations in a draft contract of sale is to elicit substantive information concerning past uses⁴⁰ and current site conditions of the property. This information can be used to assess the degree of environmental investigation necessary.⁴¹ For instance, if the current owner generates large quantities of hazardous wastes, or has a history of environmental violations, the buyer will seek more detailed information, and will be more concerned about contamination problems than if the site has had a relatively clean history.⁴²

Generally, the buyer will want to conduct some degree of

40. One source recommends investigating "as far back as possible, because some CERCLA sites involve waste generated in the last century." Fitzsimmons & Sherwood, *supra* note 11, at 775.

41. Pertinent information to assess the degree of environmental investigation necessary would include: (1) past judicial and administrative proceedings concerning the property; (2) land records resulting from land use regulations or special use permits, variances, and other authorizations; (3) securities law reports; (4) environmental reports and filings; (5) hazardous waste site lists; and (6) reports on adjacent or nearby sites. *Id.* at 775-79.

The seller should provide: (1) a detailed history of its site, of waste generated, and of waste disposal practices; (2) regulatory information (including permits, monitoring reports, etc.); (3) materials on any known spills; (4) environmental risk assessments (including any related insurance documents); (5) material on potential trouble areas such as underground storage tanks and other storage areas; and (6) chemical inventories. *Id.* at 780-81.

42. *Id.* at 781-82; Miller & Bennet, *Due Diligence Techniques for the Innocent Landowner/Purchaser*, 3 Toxics L. Rep. (BNA) 434 (Aug. 31, 1988).

site investigation in order to protect himself from liability.⁴³ As mentioned earlier, Superfund can impose strict liability on the current owner or operator of a facility for cleanup costs,⁴⁴ regardless of whether or not the current owner caused the contamination,⁴⁵ but certain statutory defenses to liability are available.

The Superfund amendments enacted in 1986 provided for an "innocent landowner" defense to Superfund liability if the buyer did not know and had no reason to know that the property was contaminated when he bought it.⁴⁶ He must demonstrate, however, that he undertook a reasonable investigation⁴⁷ of the property consistent with current commercial practices.

To qualify for the exemption, the buyer:

must have undertaken, at the time of the acquisition, all appropriate inquiry into the previous ownership and uses of the property consistent with good commercial or customary practice in an effort to minimize liability. For purposes of the preceding sentence the court shall take into account any specialized knowledge or experience on the part of the defendant, the relationship of the purchase price to the value of the property if uncontaminated, commonly known or reasonably ascertainable information about the property, the obviousness of the presence or likely presence of contamination at the property, and the ability to detect such contamination by appropriate inspection.⁴⁸

43. See generally EPA, SELECTED CURRENT PRACTICES IN PROPERTY TRANSFER ENVIRONMENTAL ASSESSMENT (1989).

44. 42 U.S.C. § 9607(a). See *supra* note 5.

45. See *New York v. Shore Realty Corp.*, 759 F.2d 1032 (2d Cir. 1985).

46. 42 U.S.C. §§ 9601(35)(A)(i), 9607(b)(3).

47. See generally H.R. 2787, 101st Cong., 2d Sess. (1989) (proposed amendment to CERCLA § 101(35) adding a new subsection C, sets forth criteria needed by a buyer to assert a rebuttable presumption that appropriate inquiry has been made regarding past use of the property); Mays, *A Practical Guide to Environmental Due Diligence in Real Estate Transactions*, 10 Hazardous Waste Rep. (BNA) No. 14, at 11 (Mar. 13, 1989).

48. Mays, *A Practical Guide to Environmental Due Diligence in Real Estate Transactions*, 10 Hazardous Waste Rep. (BNA) No. 14, at 11 (Mar. 13, 1989).

The statute indicates that, to some extent, the reasonableness of the buyer's site investigation depends on current practices in the real estate industry.⁴⁹ The extent of the investigation required will likely increase as awareness of potential environmental liabilities grows within the industry. However, at this time there is no definite standard in the industry as to what constitutes "all appropriate inquiry."⁵⁰

The EPA has issued guidelines⁵¹ which discuss the government's policy on settlement of Superfund actions against current landowners who can demonstrate that they were innocent purchasers. The requirements for settlement under the provisions of Superfund section 122(g)(1)(B) are substantially the same as the elements required for assertion of the innocent landowner defense to Superfund liability. The EPA guidelines indicate that the agency will determine what constitutes "all appropriate inquiry" on a case-by-case basis.⁵² As a result of this decision making process, there is no safe harbor defined for prospective buyers.

If the seller has already conducted a site assessment, the buyer might be satisfied to have his own consultant review the report rather than initiate an independent investigation. If the buyer's consultant raises new issues or questions the conclusions in the seller's report, the buyer might request the opportunity to undertake his own site assessment. Any reluctance by the seller to allow access to the site will likely be viewed with suspicion by the buyer. The seller should protect himself, however, by requiring the buyer to enter into an access agreement which defines the specific activities to be conducted, who is to conduct them, and at what times they will

49. For cases interpreting the innocent landowner defense, see *Washington v. Time Oil Co.*, 687 F. Supp. 529 (W.D. Wash. 1988); *United States v. Serafini*, 706 F. Supp. 346 (M.D. Pa. 1988).

50. The Federal National Mortgage Association ("Fannie Mae") has established due diligence requirements for the secondary mortgage market. *FEDERAL NATIONAL MORTGAGE ASSOCIATION, ENVIRONMENTAL HAZARDS MANAGEMENT PROCEDURES* (1988).

51. See 54 Fed. Reg. 34,235 (1989). These guidelines include guidance on landowner liability under § 107(a)(1) of CERCLA, *De Minimis* Settlements under § 122(g)(1)(B) of CERCLA, and settlements with prospective purchasers of contaminated property, See *id.*

52. *Id.*

be carried out. The agreement should protect the confidentiality of the data acquired and indemnify the seller for any damage which might be caused during the buyer's site investigation.

V. Lender's Need for Site Information

In some cases, a buyer's investigation of, and response to, environmental concerns is geared towards potential lender requirements. Banks and other institutional lenders are becoming increasingly concerned about the effects contamination has on the value of their security interests in industrial property.⁵³ As a result of this concern, some institutions require that a site assessment be conducted by their own consultants, while other institutions present the prospective borrower with an agenda for obtaining required site information.⁵⁴

There is a special exemption from Superfund liability for a secured creditor who, although technically an "owner" of a site, holds indicia of ownership primarily to protect his security interest, without participating in the management of the facility.⁵⁵ However, this protection can be lost under certain circumstances, such as when a secured lender forecloses on the property.⁵⁶ In *United States v. Maryland Bank and Trust Company*,⁵⁷ a bank held a mortgage on property originally owned by a garbage disposal company. The bank later foreclosed on the mortgage and purchased the property at the foreclosure sale.⁵⁸ A year after the foreclosure sale, the EPA discovered drums of chemicals on the property and removed them along with the surrounding contaminated soil.⁵⁹ The

53. See generally Comment, *When a Security Becomes a Liability: Claims Against Lenders in Hazardous Waste Cleanup*, 38 HASTINGS L.J. 1261 (1987).

54. See generally Ribblett & Turschmid, *Advice from Environmental Consultants: How to Achieve Competent, Comprehensive and Understandable Results from Environmental Audits*, 41 S.C.L. REV. 887 (1990).

55. 42 U.S.C. § 9601(20)(A).

56. See *United States v. Maryland Bank & Trust Co.*, 632 F. Supp. 573 (D. Md. 1986).

57. *Id.*

58. *Id.* at 575.

59. *Id.*

court ruled that the secured creditor exemption from Superfund liability was not applicable because the former mortgagee had owned the property for over a year at the time of the cleanup and no longer had only a security interest to protect.⁶⁰

A secured lender can also become potentially liable under Superfund as an "operator" of a facility by becoming overly involved in the day-to-day operations of a troubled borrower.⁶¹

The court in the *Maryland Bank* case offered specific advice to lenders for avoiding Superfund liability stating that "[m]ortgagees . . . already have the means to protect themselves, by making prudent loans. Financial institutions are in a position to investigate and discover potential problems on their secured properties. For many lending institutions, such research is routine. CERCLA will not absolve them from responsibility for their mistakes of judgement."⁶² Many lenders have heeded this advice and require environmental audits before they take security interests in industrial property.⁶³ A buyer depending on a financial institution to fund the purchase of real property may have difficulty obtaining a loan commitment if he has not obtained satisfactory information concerning environmental conditions on the property, or if contamination remains on the site at the time the property is transferred.

Lender reluctance to finance transactions in areas where even a possibility of hazardous waste contamination exists, has generated efforts to limit the Superfund liability of secured lenders. In 1989⁶⁴ and again in 1990,⁶⁵ Representative John LaFalce (D-NY) introduced a bill which provided that a

60. *Id.* at 579.

61. See *United States v. Mirabile*, [15 Litigation] *Envtl. L. Rep.* (Envtl. L. Inst.), 20,994 (E.D. Pa. 1985); *United States v. Fleet Factors Corp.*, 901 F.2d 1550 (11th Cir. 1990).

62. *Maryland Bank*, 632 F. Supp. at 580.

63. See generally Buckley, *Reducing the Environmental Impact of CERCLA*, 41 S.C.L. REV. 765, 799 (1990); Comment, *supra* note 8, at 1294.

64. H.R. Rep. No. 2085, 101st Cong., 1st Sess., 135 CONG. REC. E1325 (1989).

65. H.R. 4494, 101st Cong., 2d Sess., 136 CONG. REC. E1023 (1990).

commercial lending institution which foreclosed on real estate to protect its security interest would be excluded from the Superfund definition of "owner or operator"⁶⁶ and thus would not be liable for cleanup costs.⁶⁷

An amendment to Superfund which limited lenders' liability after foreclosure would relieve some of the anxiety currently felt by secured lenders, but would probably not eliminate lenders' request for information about environmental conditions. If mortgaged property is so contaminated as to lose a substantial portion of its market value, or if a borrower becomes insolvent as a result of environmental cleanup costs and cannot repay his loans, the lender may still suffer substantial losses. This will hold true even if lenders are not held directly liable under Superfund for cleanup costs.⁶⁸

VI. Contractual Allocation of Environmental Responsibilities

In states like New York, where there is no statute requiring environmental remediation in connection with property transfers,⁶⁹ prospective sellers often hope to find a buyer who will ask no questions but will purchase the property "as is" and indemnify and release them from all future environmental liabilities.⁷⁰ It is not surprising that such buyers are difficult to find; they would have to be willing to fund the purchase with their own money and to assume undetermined future liability for existing environmental problems. Of course, if the purchase price were low enough, such a buyer might be found. The seller also might be lucky enough to find a large company, which particularly desired his property, with sufficient expertise to evaluate and remediate likely problems and sufficient financial resources to assume the costs of any

66. 42 U.S.C. § 9601(20).

67. See *supra* note 64.

68. See Buckley, *supra* note 63.

69. *Supra* notes 15 & 35.

70. See *Mardan Corp. v. C.G.C. Music, Ltd.*, 600 F. Supp. 1049 (D. Ariz. 1984), *aff'd*, 804 F.2d 1454 (9th Cir. 1986) (in which seller received a general release of liability from the buyer). See also *FMC Corp. v. Northern Pump Co.*, 668 F. Supp. 1285 (D. Minn. 1987).

hidden liabilities.⁷¹

In many cases, however, the seller will find that the apparent benefits of an "as is" sale are illusory. As discussed previously,⁷² an "as is" provision is no insurance against Superfund liability for later cleanup costs. To the contrary, even if the buyer specifically indemnifies the seller against Superfund liabilities, the government will not recognize such an indemnification but will bring its action against all potentially responsible parties,⁷³ requiring the seller to seek reimbursement in a separate action.⁷⁴ The seller conceivably could be drawn into protracted and expensive Superfund litigation even if he was not required to pay any portion of the cleanup costs.⁷⁵ Selling contaminated property without prior remediation also increases the likelihood that existing problems will not be addressed, but will become worse instead resulting in more costly remedial efforts⁷⁶ and possibly third-party claims against the seller.⁷⁷

If the seller has not conducted a site assessment prior to entering into contract negotiations, the buyer might insist that the seller agree to investigate the property and remediate any problems prior to the closing date.⁷⁸ Such an agreement might be necessary in order to retain the potential buyer, but

71. For a recent example of difficulties incurred even when a large company agrees to assume costs, see Foderaro, *Can a Mall at a Toxic Dump Revive an Ailing Syracuse?*, N.Y. Times, Oct. 17, 1990, at B1, col. 2.

72. See *supra* notes 27-31 and accompanying text.

73. 42 U.S.C. § 9607(a) (1988).

74. 42 U.S.C. § 9613(f) provides parties with a statutory right to contribution from other PRPs in the event that they are held jointly and severally liable for damages caused by disposal of hazardous wastes. See *Lyncott Corp. v. Chemical Waste Management*, 690 F. Supp. 1409 (E.D. Pa. 1988); *Edward Hines Co. v. Vulcan Materials Co.*, 685 F. Supp. 651 (N.D. Ill. 1988).

75. See *Cadillac Fairview/California, Inc. v. Dow Chem. Co.*, [14 Litigation] *Env'tl. L. Rep. (Env'tl. L. Inst.)* 20,716 (C.D. Cal. 1984).

76. See *Nunn v. Chemical Waste Management, Inc.*, 856 F.2d 1464 (10th Cir. 1988).

77. CERCLA does not create a federal cause of action for personal injuries, but injured parties can pursue claims under state laws and common law actions. See *Sterling v. Velsicol Chem. Corp.*, 647 F. Supp. 303 (W.D. Tenn. 1986).

78. See generally Finkelstein, *Considerations Before You Buy or Lease: Avoiding a Toxic Surprise*, [Environmental Considerations in Natural Resource and Real Property Transactions] 3-1 ROCKY MTN. MIN. L. INST. (1988).

it could raise significant concerns regarding timing and the uncertainties of the amount of potential cleanup costs. If extensive environmental problems are discovered after the contract is signed, it might be very difficult to guarantee that the seller will be able to complete remedial work prior to the intended closing date. The buyer may be unwilling to extend the closing date indefinitely, and the seller will be in a very weak position for renegotiating the contract.

The seller can ensure himself a much stronger bargaining position if he conducts a site assessment prior to negotiating a contract of sale. If the property is relatively clean, the assessment will demonstrate that fact and avoid a purchase price reduction for contingent environmental liabilities. Thereafter, he will be able to negotiate the representations and indemnities⁷⁹ requested by the buyer without further investigation and facilitate a prompt sale. If the property is severely contaminated and requires notification of government agencies⁸⁰ and extensive remedial activity, the seller will be able to decide whether to address those problems without the complications of ongoing contract negotiations.

If a pre-contract site assessment reveals significant but manageable environmental problems, negotiations concerning the allocation of environmental responsibilities will be conditioned on the relative needs and strengths of the parties, the degree of contamination, and the desirability of the property if uncontaminated. One option would be for the buyer to negotiate a reduction in the purchase price and assume responsibility for the cleanup. Another option would be for the seller to set aside a specified amount of money, perhaps in an escrow fund, which the buyer could apply to post-closing cleanup expenses. The buyer would then assume responsibility for any excess costs incurred. The escrow amount could represent all, or only a portion of the estimated cleanup costs. A third option allows the seller to agree to site cleanup prior to the anticipated closing date at his own expense, with no

79. See *supra* text accompanying notes 32-39.

80. The Superfund notification requirement is contained in 42 U.S.C. § 9603(a). See *supra* note 25.

reduction in the purchase price. Even if the seller's consultant has already estimated the cost of necessary remedial work, the buyer should have his own consultant review and revise that estimate before agreeing on any purchase price reduction or escrow amount.

It is very difficult to arrive at a definite estimate of remedial costs. Cost projections depend upon the professional judgment of experienced consultants as to what actions will be necessary to accomplish the task. In addition, government cleanup standards are often indefinite and subject to change, and disposal costs increase daily. However, the information derived from a site assessment will provide some basis for estimating the probable range of anticipated remedial costs. In addition, the site assessment should alleviate some seller concerns, such as the likelihood of a Superfund cleanup claim by the EPA or by private parties. As a result, any purchase price reduction or escrow fund requested by a buyer will probably not be as great as it would be if suspected, uninvestigated environmental problems existed at the site.⁸¹

In some cases, the buyer will agree to handle remedial actions himself. However, even if the buyer assumes all responsibility for the site cleanup, the seller still will not be relieved of potential statutory liability for unremediated environmental problems.⁸² In this case, the seller will probably lose the ability to control remedial work and will run the risk that the buyer will inadequately address the problems. This creates the potential for the uncorrected contamination to create more serious risks in the future.⁸³ If the seller has identified existing contamination problems prior to negotiating the contract of sale, he would generally be well-advised to proceed with any necessary remedial work as soon as possible rather than seeking a buyer to assume the cleanup responsibility. He will often be in a better position to obtain a favorable contract

81. See generally Folkes, *Evaluating the Existence, Nature and Extent of Environmental Liabilities and Risks: Getting the Facts*, *Environmental Consideration in Real Property Transactions*, 5 ROCKY MTN. MIN. L. INST. (1988).

82. 42 U.S.C. § 9607(a)(2). See *supra* notes 42-45 and accompanying text.

83. For instance, untreated contamination may migrate off-site, or a hazardous substance may cause personal injury through contact.

price and limit remediation expenses if he controls the work himself. In addition, the sooner the work is begun, the more likely it will be completed by his desired closing date.

In those instances where the seller is going to perform the remedial work, it is generally preferred that it be completed prior to the closing date. If a lender is involved, it may want to know that the site is clean before funding the loan. The buyer may desire to begin preparing the site for his intended use as soon as possible and extensive remedial activities on the property will likely interfere with his business operations. The seller will lose control over the site after the sale is completed and might have to work around the buyer's operations, which could result in delays and increased costs. Activities by the buyer might obstruct the remedial work or cause new contamination problems for which it is difficult to allocate responsibility. In addition, the seller may well lose control over information about site conditions which might otherwise remain confidential.⁸⁴ In sum, it is better for the seller to control the performance of the remedial work with as little buyer interference as possible.

VII. Implementation and Evaluation of Private Cleanup Plans

Sellers who undertake implementation of cleanup plans without direction by a governmental agency will be relying on environmental consultants to recommend remedial measures which will meet governmental standards. Therefore, the seller must be very judicious when selecting an environmental consultant. He should seek recommendations from an environmental attorney and from others who have had experience with site remediation work including, perhaps, local governmental agencies.

The environmental consultant will not be able to propose a comprehensive cleanup plan without conducting a thorough site assessment and investigation. Depending on the site his-

84. For instance, the buyer could decide that he wants more work done than was agreed upon. He could approach governmental authorities in an attempt to direct their attention to potential areas of concern.

tory and current conditions, the evaluation process alone could require a substantial investment of time and money. The seller can expedite this process by providing the consultant with all available information about current operations as well as past uses of the property.⁸⁵ In contrast, supplying insufficient information to the consultant can result in a more expensive investigation and an incomplete cleanup plan.⁸⁶ Despite this costly result, some property owners take the position that it is the consultant's responsibility to identify potential areas of contamination and if the consultant cannot find the problem, one must not exist.

Once the environmental consultant has determined the general nature and extent of contamination in a problem area, he will be in a position to recommend appropriate treatment, removal, or containment methods. Often new information will become available, after remedial work has begun, which will require modifications or additions to the remedial plan. The consultant should be willing to certify that the site is in compliance with applicable environmental laws and regulations when and if the cleanup plan has been fully implemented. The certification would then be available to prospective buyers who would have it reviewed by their own consultants.

There are three questions commonly raised by buyers and lenders with respect to the adequacy of a seller's cleanup activities: were all environmental problems at the site identified, or was some potential source of liability overlooked;⁸⁷ were all identified problems adequately addressed;⁸⁸ and what future problems might there be if environmental laws and regulations become more restrictive.⁸⁹ All three of these questions will be factors in the buyer's requests for indemnification by the seller.

The first question can be addressed by allowing the buyer's consultant to inspect the site and determine whether

85. Ribblett & Turschmid, *supra* note 54, at 892-93; Folkes, *supra* note 81, at 5-9.

86. Ribblett & Turschmid, *supra* note 54, at 888; Folkes, *supra* note 81, at 5-9.

87. See generally Fitzsimmons & Sherwood, *supra* note 11, at 780-82.

88. See generally Ribblett & Turschmid, *supra* note 54, at 887.

89. *Id.*

additional sampling or investigation is recommended in suspected areas of concern. If the seller's consultant does not agree, the seller can offer to allow the buyer to conduct additional investigation at his own expense. If new problems are discovered, the parties will have to negotiate responsibility for any additional remedial work. Sometimes, buyers use their environmental consultant's reports as justifications for requesting additional contract price reductions. The opportunity for this can be reduced somewhat by involving both consultants in the contract discussions so that technical issues can be addressed on a face-to-face basis.

The second question is also a matter for review and discussion between the consultants. The Environmental Protection Agency and some state agencies have established acceptable levels for certain hazardous contaminants based on health risk assessments, but for many potentially harmful chemicals there is no established level to which remedial action is required. "How clean is clean" is a question which arises even in government-directed cleanups.⁹⁰ In New York, if there is no EPA level established, consultants sometimes look to cases decided in New Jersey. The New Jersey cases are most often based upon implementing ECRA⁹¹ site cleanups. In these cases, there is no definitive standard by which one can determine that a contaminated site should now be considered clean.

The third question is related to the second. Government standards for acceptable risks are increasingly restrictive and as new information becomes available, additional chemicals become subject to regulation.⁹² Generally, the seller will not volunteer to clean up the sale property beyond levels specifi-

90. CERCLA itself does not contain any statutory cleanup standards. Cleanup levels are determined on a site-by-site basis and must comply with the requirements of other federal and state environmental laws which are "applicable or relevant and appropriate." 42 U.S.C. § 9621(d)(2)(A).

91. See *supra* note 14.

92. For instance, a number of new chemicals became subject to regulation effective September 25, 1990, as a consequence of the EPA's promulgation of the Toxicity Characteristic Leaching Procedure as one of the criteria for determining the characteristics of hazardous wastes. 55 Fed. Reg. 11,798 (1990); 55 Fed. Reg. 26,986 (1990).

cally required under current regulations. Similarly, the buyer will not want to remedy problems caused by the prior owner when new regulations are issued. Information supplied by consultants can help define the risk of future regulatory obligations, but will not provide the degree of certainty desired by buyers and their lenders.

VIII. Indemnification Issues Remaining After Remedial Work

A buyer will usually seek seller indemnification against any liabilities resulting from the presence of any pre-existing contamination at the time of the sale.⁹³ The seller will retain statutory liability for cleanup costs,⁹⁴ but the buyer may want additional contractual protection covering all manner of potential losses, including penalties, fines, expenses, damages, private party claims, lost profits, business interruption, and attorneys fees.

The seller may be required to provide some form of indemnification to the buyer, but he will be able to limit his future exposure more completely, if he has completed a site assessment and implemented a cleanup plan prior to negotiating the contract of sale.⁹⁵ Both the seller and the buyer will have much greater assurance that site conditions will not result in Superfund liability or otherwise require extensive additional remedial work. As a result of this assurance, the seller will be in a stronger position to negotiate limitations on indemnity provisions requested by the buyer.

There may be cases where the seller has implemented a cleanup plan but the buyer is concerned that the remedial work might not have been extensive enough to address known contamination problems. In these instances, the buyer might be satisfied with an indemnification which is limited to a rela-

93. See generally Dore, *A Practical Guide to Environmental Indemnification Agreements*, 55 DEF. COUNS. J. 297 (1988).

94. 42 U.S.C. § 9607(a)(2).

95. See generally Bleicher & Stonelake, *Caveat Emptor: The Impact of Superfund and Related Laws on Real Estate Transactions*, 14 Env'tl. L. Rep. (Env'tl. L. Inst.) 10,017 (1984); Fitzsimmons & Sherwood, *supra* note 11, at 765.

tively short period of time after the sale, during which time he can investigate the problem and determine whether additional work is needed.⁹⁶ If specific issues were raised by the buyer's consultant regarding potential inadequacies in the cleanup plan, it should also be possible to estimate the approximate costs of addressing those concerns. This estimate will provide a reasonable basis for limiting the dollar amount of the proposed indemnification. In any event, some sort of cost sharing device would help discourage the buyer from incurring unnecessary costs.⁹⁷

If the buyer is concerned about unknown and therefore unremediated site conditions, he should be reassured somewhat by the fact that a thorough site investigation was undertaken by the seller's consultant, and perhaps by his own as well. Even if the seller provides some indemnification against unknown liabilities, the buyer will probably be satisfied with a shorter period of time and a smaller dollar amount than if site conditions had not been investigated and addressed.⁹⁸

Unless the parties are aware of specific proposed regulatory changes which would affect the sale property, the seller should oppose accepting responsibility for the costs of complying with future environmental laws or regulations. Once known contamination of the property has been cleaned up to currently acceptable levels, the buyer is not likely to confront the sorts of completely uncontrolled hazards that Superfund was enacted to address and should not need the same degree of protection against future regulatory requirements as he would if the property were currently unregulated and unremediated. Few industrial sites are free of all potential hazards, however, and it is impossible to predict accurately what sorts of environmental concerns will emerge in the future. Buyers will therefore rarely be willing to accept the entire risk of future compliance costs with respect to environmental problems they did not create.

96. Dore, *supra* note 93, at 300.

97. See generally Fitzsimmons & Sherwood, *supra* note 11, at 789-90.

98. *Id.* See generally Folkes *supra* note 81.

IX. Conclusion

Given the current level of environmental awareness and regulation, cleaning up contaminated industrial property is not only good policy, it is good business. In many cases it will help a property owner to sell his site quickly, for a good price, with the least exposure to later environmental costs and liabilities. It requires a substantial commitment of resources, but if the environmental problems are not too severe, the enhanced market value of the property will often outweigh the cost of the remedial effort.

New York State has considered enacting a land transfer statute which would require a seller of nonresidential property to present the buyer, prior to transfer, with either a certification of noncontamination or a certification of planned remedial action.⁹⁹ Given the private market pressures already impelling sellers to conduct pre-sale environmental assessments and, if necessary, site cleanups, it is questionable whether such legislation would substantially improve the current situation.

99. See *supra* note 15.