

Bona Fide Prospective Purchaser Defense under CERCLA: Post-Closing Concerns and Tenant Issues Update

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We are nearing the 10-year anniversary of the bona fide prospective purchaser (BFPP) defense, and still many questions abound regarding the use of the defense. Recent cases and guidance from the U.S. Environmental Protection Agency (EPA) help shed some light on some of the more material issues.

In 2010, district courts in California and South Carolina considered whether a defendant was in fact a BFPP with the determination based upon the post-closing actions of the defendant rather than the pre-closing due diligence. Additionally, EPA issued guidance in 2009 that is helpful for tenants in determining if they qualify as BFPPs. This article explores the recent decisions and guidance, and how they may affect those who desire to rely on the BFPP defense.

Phase I Environmental Site Assessments

The Small Business Liability Relief and Brownfields Revitalization Act (Brownfields Act) signed into law by President Bush on Jan. 11, 2002, amended the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA) to help stimulate the redevelopment of Brownfields. One of the requirements was for the EPA to develop its own Phase I environmental site assessment criteria called "all appropriate inquiries" (AAI).¹ On Nov. 1, 2005, EPA published its AAI rule. The most important aspect of the AAI rule was that it specifically provided that a then new version of the ASTM "Phase I Site Assessment Process Standard" E 1527-05 (2005 ASTM Standard) may be used to meet AAI. Since the AAI rule went into effect, most Phase Is have been performed following the 2005 ASTM Standard.

Bona Fide Prospective Purchasers

With the enactment of the Superfund Amendments and Reauthorization Act (SARA) in 1986 amending CERCLA came the "innocent purchaser defense." This allowed potential purchasers the ability to purchase property after performing a Phase I environmental site assessment, provided no concerns for releases for hazardous substances were identified. If a potential concern were found, then a purchaser either had to walk away from the purchase or understand that upon closing it would become an owner or operator under CERCLA and have liability for the contamination on the site. This was a material impediment to the purchase and redevelopment of Brownfields in particular.

The creation of the BFPP defense was meant to help alleviate this issue. In very simplistic terms, the BFPP defense allows a purchaser to conduct AAI and to purchase property with knowledge of hazardous substance contamination without incurring liability as an owner or operator. Many purchasers though do not focus on the additional requirements beyond AAI that must be met to maintain BFPP status.

A BFPP is defined as "a person (or a tenant of a person)" that acquires ownership of a facility after the release of the hazardous substances and after Jan. 11, 2002, who meets the following criteria:

- Conducted "all appropriate inquiries" into the previous ownership and uses of the property.
- The disposal of hazardous substances on the site occurred before acquisition.
- Provide all legally required notices regarding the release.
- Provide full cooperation, assistance and access to those conducting response actions.

¹ 40 C.F.R. pt. 312.

- Comply with institutional and engineering controls and do not impede the effectiveness.
- Comply with governmental requests for information and subpoenas.
- Not already liable, affiliated with a responsible party “(other than a contractual, corporate or financial relationship that is created by the instruments by which title to the facility is conveyed or financed or by a contract for the sale of goods or services)” or simply the reorganized entity of a responsible party.
- Exercise appropriate care with respect to the hazardous substances found – stop continuing release, prevent threatened future release, and prevent exposure.

BFPP Defense Analyzed by Courts

With the great fan fare that accompanied EPA’s AAI in 2005, the focus quickly became meeting AAI with the ongoing obligations to remain a BFPP slipping to the background. Two recent cases regarding the BFPP defense may change the focus back to what is found in the Phase I and not just completing it as both cases were decided based upon the post-closing acts or omissions of the purchasers.

3000 E. Imperial, LLC v. Robertshaw Controls Co.

In *3000 E. Imperial, LLC v. Robertshaw Controls Co.* (C.D. CA 2010),² the court focused on the “appropriate care” component of the BFPP defense. *3000 E. Imperial, LLC* (Imperial) purchased a property in Lynwood, Calif., on Nov. 30, 2006. Investigations prior to the purchase identified soil and ground water contamination primarily from trichloroethylene (TCE) and benzene. A manufacturing facility, a lumber and hazardous materials storage shed, and a maintenance shed were demolished in 2007 leaving “a vacant concrete lot.” Underground storage tanks were installed on the property in 1942.

Imperial brought suit against a former owner, Robertshaw Controls Co., seeking among other relief, response costs under CERCLA. Robertshaw Controls Co. brought a counterclaim for contribution claiming that Imperial was liable as the current owner and operator of the property. Imperial asserted its defense to liability as a “bona fide prospective purchaser whose potential liability for a release or threatened release is based solely on the purchaser's being considered to be an owner or operator of a facility shall not be liable as long as the bona fide prospective purchaser does not impede the performance of a response action or natural resource restoration.”³

The court noted that Imperial cooperated with the California Department of Toxic Substances (DTSC) to coordinate a voluntary cleanup of the site beginning in May 2007, and that the DTSC had found that Imperial was a BFPP under California law. The stated notes that while the requirements for a BFPP are similar under California law and CERCLA, the definition of appropriate care is different. In California, it means performance of response actions directed by the DTSC, which is what Imperial was doing. CERCLA has a broader definition requiring “reasonable steps to (i) stop any continuing release; (ii) prevent any threatened future release; and (iii) prevent or limit human, environmental, or natural resource exposure to any previously released hazardous substance.”⁴

Imperial had the contents of the underground storage tanks sampled in May 2007. The consultant reported that the contents contained TCE in September 2007. Imperial

² LEXIS 138 661.

³ 42 U.S.C. § 9607(r).

⁴ 42 U.S.C. § 9601(40)(D).

pumped the contents from the tanks in October 2007, then removed the tanks in 2009. The court determined that since Imperial removed the contents of the tanks shortly after learning that they contained TCE, that it had exercised appropriate care and was a BFPP. What is unclear from the case is whether the tanks were identified in the Phase I. If they were identified, it would seem that appropriate care would require sampling when they were identified to be able to exercise appropriate care beginning upon learning of the presence of the tanks. If they were not identified in the Phase I, there would be a question whether the consultant actually completed AAI correctly.

Ashley II of Charleston, LLC v. PCS Nitrogen, Inc.

In *Ashley II of Charleston, LLC v. PCS Nitrogen, Inc.* (S.C. 2010)⁵, the court also considered the assertion by a party that it qualified as a BFPP with a very long and complicated set of facts. The property at issue is a 43-acre tract on the Ashley River in Charleston, S.C., that operated as a former fertilizer manufacturing facility. The site has lead, arsenic and carcinogenic polyaromatic hydrocarbon contamination as well as low pH. Ashley II of Charleston, LLC (Ashley) purchased a portion of the site in 2003. Ashley tore down a building exposing a number of cracked sumps containing hazardous substances. This allowed the sumps to fill with rain water and impact the site. The court concluded that Ashley failed to prove a requirement for the BFPP defense that all disposal occurred before Ashley acquired the site, because the evidence supported that the sumps would have leaked after Ashley's purchase.

The court also found that Ashley failed to exercise appropriate care in three instances. First was tearing down the building and exposing the cracked sumps containing hazardous substances to rain water. Second, although Ashley installed security fences around the property, the gates were not kept locked for a period of time. This allowed dumping of debris to occur. Ashley failed to investigate the debris and to remove the debris pile for more than a year. Third, Ashley failed to maintain "a limestone run of crusher (ROC) layer that is graded to promote better drainage" over the site allowing it to erode exposing contaminated soil.

One other element the court found that Ashley failed to meet was having no affiliation with a potentially responsible party. Ashley released and indemnified two sellers to Ashley who were found to be potentially responsible parties. Ashley attempted to persuade EPA not to take enforcement action against such parties. The court found that "Ashley's efforts to discourage EPA from recovering response costs covered by the indemnification reveals just the sort of affiliation Congress intended to discourage," and therefore that Ashley could not meet this component of the BFPP defense.

The court's finding that disposal occurred after Ashley acquired the site is troubling. In order to protect against this, a purchaser would need to take actions prior to closing to empty and secure any vessels that might release hazardous substances such as tanks, sumps or drums. It would not be enough to promptly act post closing to address the concern based upon the court's finding. Another concern is the court's analysis of Ashley's actions to discourage EPA from pursuing parties that Ashley had agreed to indemnify. The BFPP defense specifically identifies a "contractual, corporate or financial relationship that is created by the instruments by which title to the facility is conveyed or financed" as not creating an affiliation.⁶

Additionally, CERCLA provides that "[n]o indemnification, hold harmless, or similar agreement or conveyance shall be effective to transfer from the owner or

⁵ LEXIS 104772.

⁶ 42 U.S.C. § 9601(40)(H)(i)(II).

operator...liability imposed under this section.”⁷ The Ashley court though makes it clear that a purchaser planning to use the BFPP defense should not advocate for another responsible party regarding liability at the site. A purchaser should carefully consider whether it should indemnify or assume the liability of its seller who may be a responsible party. Such assumption negates the benefits of the BFPP defense analysis as whether a BFPP or not the purchaser would have the liability contractually.

Tenants as BFPPs

Although the BFPP defense in its basic form is for a “purchaser,” EPA issued guidance in early 2009 providing for two ways that a tenant may be a BFPP. The guidance document, “Enforcement Discretion Guidance Regarding the Applicability of the Bona Fide Prospective Purchaser Definition in CERCLA Section 101(40) to Tenants” (Tenant BFPP Policy), provides that EPA will exercise enforcement discretion against tenants in the following categories:

1. A tenant whose lease gives sufficient indicia of ownership to be considered an “owner” and who meets the elements of §§ 101(40)(A)-(H) and 107(r)(1).
2. A tenant of an owner who is a BFPP.

The guidance relies on the 2000 case of *Commander Oil v. Barlo Equip. Corp.*⁸ for criteria as to when a tenant may be an “owner” under CERCLA. The *Commander Oil* court considered whether a tenant had such extensive responsibilities under a lease that the tenant held sufficient “indicia of ownership” to be considered an owner of the property. The court focused on the responsibilities of the tenant, the ability of the tenant to make decisions concerning the property, the length of the lease, the range of permitted uses, the reservation of rights of the owner, and who was responsible for paying taxes and insurance and making repairs. EPA provides in the Tenant BFPP Policy that it will consider such factors as to whether the tenant holds sufficient indicia of ownership to be an owner in exercising its enforcement discretion regarding the tenant being a BFPP.

The other instance where a tenant can be a BFPP is derived from the definition of BFPP under CERCLA, which includes a “tenant of a bona fide prospective purchaser.”⁹ The key is whether the landlord conducted AAI when the landlord purchased the property and continues to meet the requirements of a BFPP. It is a somewhat unusual aspect of the defense as it does not provide for the lease to be contemporaneous with the purchase. The landlord could have met the requirements in a purchase any time after Jan. 11, 2002, when the defense was added to CERCLA pursuant to the Brownfields Act.

Additionally, the BFPP Tenant Policy provides that this derived defense to liability from the landlord requires that the tenant must not:

1. Dispose of hazardous substances or exacerbate existing hazardous substance contamination at the facility, or
2. Impede the performance of a response action or natural resource restoration.

If a tenant hopes to assert the BFPP defense, it will need to assess whether its landlord met AAI upon its purchase and has followed the BFPP requirements post closing like Imperial or failed to meet the requirements like Ashley. A tenant would need to complete extensive due diligence before becoming obligated under the lease as a

⁷ 42 U.S.C. § 9607(e).

⁸ 215 F.3d 321 (2d Cir. 2000),

⁹ 42 U.S.C. § 9601(40).

tenant. Upon entering into the lease, the tenant should take steps to assure that it also meets the requirements of the EPA guidance to maintain its own BFPP protection. The tenant will also need to monitor the landlord's ongoing compliance with the BFPP requirements and may need to have some rights to step in to address concerns in certain instances. Having control may tip the scale to the tenant being an "owner" such as in *Commander Oil*, so the tenant should meet AAI prior to entering into the lease so that it may assert that it is in one of the two categories of tenant eligibility? to be a BFPP under the BFPP Tenant Policy.

Conclusion

A purchaser or tenant desiring to be a BFPP needs to do much more than just complete a Phase I. The *3000 E. Imperial* and *Ashley* cases as well as the BFPP Tenant Policy highlight the need for purchasers or tenants of contaminated property to take precautions after the purchase or lease if they intend to be protected from liability as BFPPs.

For more information on the BFPP defense, please contact Jim Thornhill at 804.775.1163 or jthornhill@mcguirewoods.com.